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Vol. II Company Accounts & Analysis of Financial Statements

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Along with Project Work

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6. Company Accounts — Issue of Shares 6.1 — 6.208

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7. Company Accounts — Issue of Debentures 7.1 — 7.74

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9. Financial Statements of Companies 9.1 — 9.82

10. Financial Statement Analysis (Theory) 10.1 — 10.12

11. Tools for Financial Analysis : Comparative Statements 11.1 — 11.40

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13. **Cash Flow Statement** 13.1 — 13.167

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14. **Ratio Analysis** 14.1 — 14.184

For additional Illustrations and Questions Scan the QR Code or **Enter the following URL on your web browser :** http://qr.apcbooks.co.in/575628/

PROJECT WORK P-1 — P-82

ISC Annual Examination Paper 2018 QP-1 — QP-9

ISC Annual Examination Paper 2019 QP-10 — QP-20

ISC Annual Examination Paper 2020 QP-21 — QP-30

Answers of Multiple Choice Questions A-1 — A-14

6

Company Accounts — Issue of Shares

LEARNING OBJECTIVES

After studying this Chapter you should be able to understand :

- **Meaning and Characteristics of a Company**
- **Meaning, Nature and Types of Shares**
- **Distinction between Preference Share and Equity Share**
- **Meaning, Nature and Types of Share Capital**
- **Distinction between Reserve Capital and Capital Reserve**
- **Issue and Allotment of Shares**
- **Public Subscription of Share Capital**
- **Issue of Shares at Par and at a Premium**
- **Issue of Shares for Consideration other than Cash**
- **Calls in arrear and interest thereon**
- **Calls in advance and interest thereon**
- **Over-Subscription and Under-Subscription**
- **Forfeiture and Re-issue of Shares**

Sole proprietorship and partnership forms of business organisations could not meet the growing demands of a very big business, because of their limitations such as limited capital, limited managerial ability, unlimited liability and other drawbacks. Therefore, a Company form of business organisation came into existence to do away with the defects of sole proprietorship and partnership forms of business organisations.

A Company is a voluntary association of persons formed through the process of law, for the purpose of carrying on some business.

Definitions :

Lord Justice Lindley defines a Company as follows, ''It is an association of persons who contribute money or money's worth to a common stock and employ it for some common purpose.''

''A Company is an artificial person created by law, having separate entity with a perpetual succession and a common seal''. — **Prof. Haney**

Characteristics (Features) of a Company :

Following are the essential characteristics of a Company :

(1) **Separate Legal Entity :** A Company is a legal person and its entity is quite distinct and separate from its members. It can purchase and sell the properties in its own name, can open bank account in its own name and can enter into contracts. Since a Company has a legal personality distinct from that of its members, a creditor of such a Company can sue only the Company for his debts and not any of its members.

(2) **Perpetual Existence :** The existence of a Company is not affected by the retirement, death, lunacy or insolvency of its members. Shareholders may come and Shareholders may go but the Company goes on for ever, unless wound up according to Companies Act.

(3) **Limited Liability :** The liability of the shareholder of a Company is limited to the unpaid value of his shares. For example, if the face value of a share in a Company is ₹10 and a shareholder has already paid ₹8 per share, he can be called upon to pay not more than ₹2 per share.

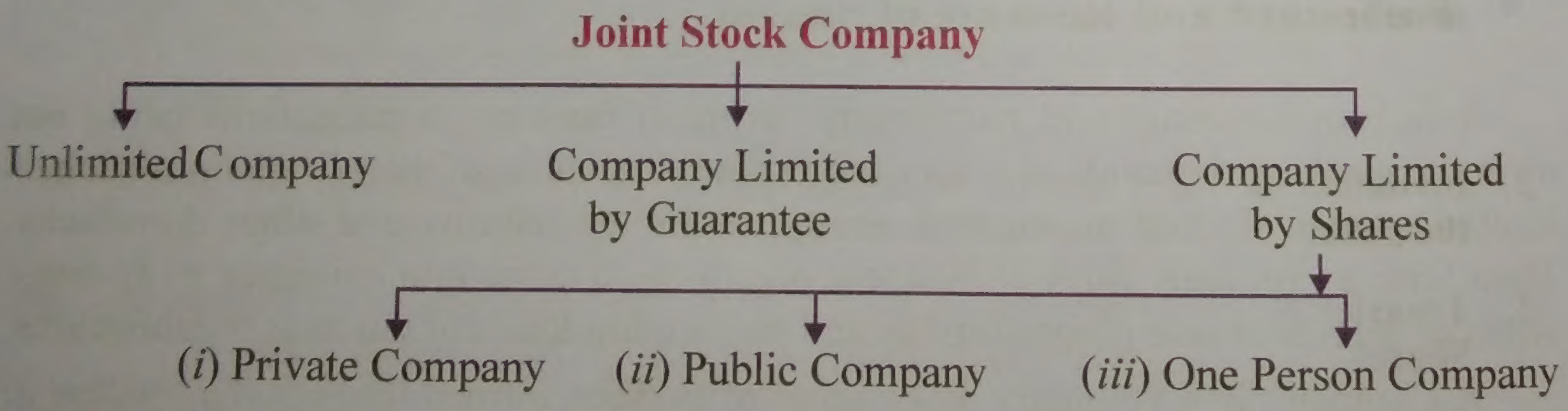
(4) **Common Seal :** A Company may or may not maintain a common seal. If it has a common seal, it is affixed to all the important documents of the Company.

(5) **Transferability of Shares :** The Capital of the Company is divided into parts, called shares. These shares are freely transferable subject to certain conditions.

(6) **Separation of Management from Ownership :** Shareholders are the true owners of a Company, but usually, the number of shareholders is quite large, and as such it is neither possible nor desirable for each member to take part in the day-to-day management of the Company. Therefore, the Company is managed by a 'Board of Directors' elected by the shareholders.

Kinds of a Company

Companies registered under the Companies Act, 2013, may be classified as below:


Joint Stock Company
Unlimited Company
Company Limited by Guarantee
Company Limited by Shares
(*i*) Private Company
(*ii*) Public Company
(*iii*) One Person Company

Unlimited Company : Unlimited Company is a company where there is no limit on the liability of its members. It means, when a company suffers loss and the company's property is not sufficient to pay off its debts, the private property of its members will be used to meet the claims of creditors. As the risk involved in such companies is too high, these are not found in India even though permitted by the Companies Act.

Company Limited by Guarantee : In case of such a company, the liability of the members is limited to the extent of the guarantee given by them in the event of the winding up of the company. The liability of its member will arise only in the event of winding up of the company.

Company Limited by Shares : In case of such a company the liability of the members is strictly limited to the extent of the nominal value of shares held by each of them. If a member has already paid the full amount of the shares, he will not be liable to pay any amount. If a member has partly paid shares, he can be forced to pay the remaining amount during the existence of the company as well as during the winding up. Such companies may be sub-divided into private, public and one person companies:

(*i*) Private Company :

As per Section 2 (68) of the Companies Act, 2013, a private company is one which by its Articles of Association

(*i*) restricts the right to transfer its shares;

(*ii*) limits the number of its members to 200 (exclusive of past and present employees);

(*iii*) prohibits any invitation to the public to subscribe for any securities *i.e.,* shares or debentures of the company.

The name of every private company must end with the words 'Private Limited'.

(*ii*) Public Company :

As per Section 2 (71) of the Companies Act, 2013, a public company means a company which is not a private company.

DISTINCTION BETWEEN PRIVATE COMPANY AND PUBLIC COMPANY

Basis of Distinction	*Private Company*	*Public Company*
1. **Number of members**	Minimum number of members is 2, and the maximum, exclusive of past and present employees, is 200.	Minimum number of members is 7 and there is no limit to maximum number.
2. **Invitation to the public**	It cannot invite the public to subscribe to its shares.	It can invite the public to subscribe to its shares.
3. **Transfer of Shares**	There is restriction on the transfer of its shares.	There is no restriction on the transfer of its shares.
4. **Preparation of Articles**	Preparation of Articles is necessary for all private companies.	Preparation of Articles is not necessary. In case the Articles are not registered, the provisions of Table F of Schedule I given in Companies Act 2013 shall apply.
5. **Number of Directors**	It must have at least two directors.	It must have at least three directors.
6. **Use of word 'Limited'**	It is compulsory to use the words 'Private Limited' at the end of its name.	Only the word 'Limited' is used at the end of its name.

(*iii*) One Person Company OR OPC :

Meaning :

Companies Act 2013 introduces a new type of entity to the existing list i.e., apart from forming a public or private limited company, the Act enables the formation of a new entity 'One Person Company' (OPC). An OPC means a private limited company with only one person as its member [Section 2 (62)]. Following rules are applicable on OPC :

1. **Member of OPC :** Only a natural person who is an Indian citizen and resident in India can be a member of OPC.

   The term 'Resident in India' means a person who has stayed in India for a period of not less than 182 days immediately preceding one calendar year.
2. One person can form only one OPC.
3. Its paid up Share Capital should not exceed ₹50 Lakh.
4. Its average annual turnover of three years should not exceed ₹2 Crore.
5. **Purpose :** As per Rule 3 (5) of Companies (incorporation) rules 2014, an OPC cannot be formed for charitable purposes. In other words, it can be formed for business purpose only.
6. **Conversion :** An OPC cannot convert itself into public or private company unless a period of 2 years has expired from the date of its incorporation and conversion is mandatory when the paid-up share capital is increased beyond ₹50 Lakh or its average annual turnover during the relevant period exceeds ₹2 Crore.

Benefits :

(*i*) OPC is not required to include Cash Flow Statement in its financial statements.

(*ii*) The provision relating to calling of AGM, Notice for General Meeting, Quorum for meetings, Proxies etc. shall not apply to OPC.

In this chapter, problems relating to issue of shares have been discussed in detail. But before solving the practical questions relating to issue of shares, it is necessary to understand the meaning of share, types of shares and the method of their issue.

Shares :

Meaning of Shares : Total Capital of the Company is divided into units of small denominations. Each such unit is called 'share'. For example, if the total capital of the Company is ₹10,00,000, divided into 1,00,000 units of ₹10 each, each unit of ₹10 will be called a share (of ₹10 each). Thus in the above case the Company has 1,00,000 shares of ₹10 each. Shares must be numbered so that they may be identified.

Nature of Shares : The shares of a Company are movable property, transferable in the manner provided by the Articles of Association of the Company. Shares of a Company are treated as goods under the Sales of Goods Act, 1930. These can be bought, sold, hypothecated and bequeathed.

Classes, Kinds or Types : Under Section 43 of the Companies Act, 2013, a Company may issue two types of shares :

(1) Preference Shares

(2) Equity Shares

(1) **Preference Shares :** Preference Shares are those which carry the following two rights :

(*i*) They have a right to receive dividend at a fixed rate before any dividend is paid on the equity shares.

(*ii*) When the company is wound up, they have a right to the return of capital before that of equity shares.

In addition to the above, the preference shares may carry some more rights such as the right to participate in excess profits when a specified dividend has been paid on the equity shares or the right to receive a premium at the time of redemption.

Types of Preference Shares :

(*i*) **Cumulative Preference Shares :** Cumulative preference shares are those preference shares, the holders of which are entitled to recover the arrears of preference dividend, before any dividend is paid on equity shares. This means that if in any year, the profits of the company are insufficient to pay dividend on these shares, the dividend keeps on accumulating until it is fully paid. For example, if dividend has not been paid for the years ending 31st march 2018 and 2019 on 8% cumulative preference shares and the company wants to distribute dividend on equity shares for the year ending 31st March 2020, a total of 24% dividend (for the years ending 31st March 2018, 2019 and 2020) will have to be first paid on preference shares before the payment of any dividend to equity shares. The arrears of dividend on these shares are shown in the balance sheet as a commitment under 'Contingent Liabilities and Commitments'.

(*ii*) **Non-cumulative Preference Shares :** The holders of such shares get a fixed amount of dividend out of the profits of each year. If no dividend is declared in any year due to any reason, such shareholders get nothing, nor can they claim unpaid dividend of any year in any subsequent year.

(*iii*) **Participating Preference Shares :** Such shares, in addition to the fixed preference dividend, carry a right to participate in the surplus profits, if any, after dividend at a stipulated rate has been paid to equity shareholders. Similarly, in the event of winding up, if after paying back both the preference and equity shareholders, there is still some surplus left, such shareholders are entitled to receive a pre-determined proportion of surplus.

(*iv*) **Non-participating Preference Shares :** Such shares get only a fixed rate of dividend every year and do not carry a right to participate in the surplus profits or in any surplus on winding up. Unless expressly provided, the preference shares are usually non-participating.

(*v*) **Redeemable Preference Shares :** Such shares are those which will be repaid by the Company within a stipulated period in accordance with the terms of issue and the fulfilment of certain conditions laid down in Section 55 of the Companies Act 2013.

(vi) **Irredeemable Preference Shares :** Irredeemable preference shares are those, the capital of which cannot be refunded before winding up. According to Section 55, no company limited by shares, can issue any preference share, which is irredeemable or is redeemable after the expiry of 20 years from the date of its issue.

(vii) **Convertible Preference Shares :** Holders of these shares have a right to get their preference shares converted into equity shares at their option according to the terms of issue.

(viii) **Non-Convertible Preference Shares :** When the holders of preference shares have not been conferred the right of getting their preference shares converted into equity shares, such shares are called non-convertible preference shares.

(2) **Equity Shares :** Equity shares are those shares which are paid dividends only when profits are left after the preference shareholders have been paid fixed rate of dividends. In other words, there will be no fixed rate of dividend on the equity shares. If in a particular year, there are no profits or insufficient profits, the equity shares will receive nothing. If the Company earns more profits, they get a higher rate of dividend. As regards return of capital, equity share capital is returned only when preference share capital is returned in full. Equity shareholders have voting rights and control the affairs of the Company.

DIFFERENCE BETWEEN PREFERENCE SHARES AND EQUITY SHARES

Serial No.	*Basis of Distinction*	*Preference Shares*	*Equity Shares*
1.	**Rate of Dividend**	Preference Shares are paid dividend at a fixed rate.	The rate of dividend on equity shares is not fixed. It may vary from year to year depending upon the availability of profits.
2.	**Arrears of dividend**	If dividend is not paid on these shares in any year, the arrears of dividend may accumulate.	In case of equity shares, dividend cannot accumulate.
3.	**Preferential right as to the payment of dividend**	They have a right to receive dividend before any dividend is paid on equity shares.	Payment of dividend on equity shares is made after the payment of preference dividend.
4.	**Preferential right as to the payment of capital**	They have a right to return of capital in the case of winding up, before any capital is returned to equity shareholders.	Equity share capital is paid only when preference share capital is paid out fully.
5.	**Voting rights**	Preference Shareholders do not have any voting rights.	Equity Shareholders enjoy voting rights.
6.	**Right to participate in management**	They do not have a right to participate in management of the Company.	They have full right to participate in management of the Company.

SHARE CAPITAL

Meaning : Share Capital means the Capital raised by a Company by the issue of shares. Many individuals and institutions contribute varying sums to the Company's capital yet there is no separate Capital Account for each of these individuals or institutions. There is one Consolidated Capital Account called the Share Capital Account.

Kinds of Share Capital : The various terms used in connection with the Share Capital of a company are the following :

(1) **Authorised, Registered or Nominal Capital :** Authorised Capital refers to that amount which is stated in the Memorandum of Association. This is the maximum Capital for which a Company is authorised to issue shares during its lifetime.

(2) **Issued Capital :** Issued Capital is that part of Authorised Capital which is offered to the public for subscription. The remaining part of the Authorised Capital is known as the 'Unissued Capital' which can be issued later on.

(3) **Subscribed Capital :** Subscribed Capital is that part of Issued Capital which has been subscribed for by the public. If, say, 13,000 shares of ₹100 each are offered to the public and the public applies for 12,000 shares, the Subscribed Capital will be ₹12,00,000.

Subscribed capital is shown in the Balance Sheet under two heads :

(*a*) Subscribed and fully paid up; and

(*b*) Subscribed but not fully paid up.

(*a*) **Subscribed and fully paid up :** When entire nominal (face) value of a share is called by the company and also paid up by the shareholder, it is said to be 'Subscribed and fully paid-up' Capital. It is shown in the balance sheet in the following manner :

ILLUSTRATION 1.

The authorized capital of Ruchi Ltd. is ₹25,00,000 divided into 2,50,000 equity shares of ₹10 each. Out of these, the company issued 1,00,000 equity shares for subscription to the public.

The public applied for 90,000 equity shares and all the money was duly received. How will you show the 'Share Capital A/c' in the Balance Sheet of the company? Also prepare 'Notes to Accounts' for the same.

SOLUTION :

EXTRACT OF BALANCE SHEET OF RUCHI LTD.

As at ....

Particulars	*Note No.*	*Amount current year*	*Amount previous year*
I. EQUITY AND LIABILITIES :		₹	₹
Shareholder's Funds :			
(*a*) Share Capital	1	9,00,000	

Notes to Accounts :

	₹
(1) **Share Capital :**	
Authorised Capital :	
2,50,000 Equity Shares of ₹10 each	25,00,000
Issued Capital :	
1,00,000 Equity Shares of ₹10 each	10,00,000
Subscribed & Full Paid	
90,000 Equity Shares of ₹10 each	9,00,000

(*b*) **Subscribed but not fully paid up :** Shares are said to be 'Subscribed but not fully paid-up' under the following two situations :

(*i*) When the company has called-up the full nominal value of the share but the shareholder has not paid some part of the nominal value of the share.

(*ii*) When the company has not called-up the full nominal value of the share.

ILLUSTRATION 2.

X Ltd. was registered with an authorised capital of 2,00,000 equity shares of ₹10 each. The company offered 1,50,000 shares to the public for subscription at a premium of 20%. Applications for 1,45,000 shares were received and allotment was made to all the applicants. All calls were made and were duly received except the final call of ₹3 on 5,000 shares.

Present the Share Capital in the Balance Sheet of the company as per Schedule III, Part I of the Companies Act, 2013.

SOLUTION :

X Ltd.

EXTRACT OF BALANCE SHEET *as at* ....

Particulars	*Note No.*	*Current year*	*Previous year*
I. **EQUITY AND LIABILITIES :**		₹	₹
Shareholder's Funds :			
(*a*) Share Capital	1	14,35,000	

Notes to Accounts :

	₹
(1) **Share Capital :**	
Authorised Capital :	
2,00,000 Equity Shares of ₹10 each	20,00,000
Issued Capital :	
1,50,000 Equity Shares of ₹10 each	15,00,000

Subscribed Capital :			
Subscribed and Fully Paid Capital :			
1,40,000 Equity Shares of ₹10 each fully called up		14,00,000	
Subscribed but not Fully Paid Capital :			
5,000 Equity Shares of ₹10 each fully Called up	50,000		
Less : Calls in Arrears (5,000 Shares × ₹3)	15,000	35,000	14,35,000

IMPORTANT NOTE

Only the disclosure of Share Capital in a Company's Balance Sheet is a part of the syllabus. Hence, the disclosure of Securities Premium in the Balance Sheet is not required.

ILLUSTRATION 3.

Sharp Ltd. was formed on 1st December, 2013, with a capital of ₹5,00,000 divided into shares of ₹10 each. It offered 80% of the shares to the public.

The issue price was payable as follows :

30% of the face value per share was payable with application.

20% of the face value per share was payable with allotment.

The balance as and when required. The company did not call for the balance during the year.

All the shares offered by the company were subscribed for. The company did not receive the allotment money on 3,000 shares.

You are required to :

(*i*) Show the Share Capital in the Balance Sheet of the Company (prepared as per Schedule III of the Companies Act, 2013) at the end of the financial year.

(*ii*) Prepare Notes to Accounts. *(I.S.C. 2014)*

SOLUTION :

EXTRACT OF BALANCE SHEET OF SHARP LTD.

as at 31st March, 2014

Particulars	*Note No.*	*31st March, 2014*	*31st March, 2013*
I. EQUITY AND LIABILITIES :		₹	₹
Shareholder's Funds			
(*a*) Share Capital	1	1,94,000	

Notes to Accounts :

	₹
(1) Share Capital	
Authorised Capital :	
50,000 Equity Shares of ₹10 each	5,00,000

Issued Capital : 40,000 Equity Shares of ₹10 each		4,00,000
Subscribed but not fully paid Capital : 40,000 Equity Shares of ₹10 each, ₹5 called up	2,00,000	
Less : Calls in Arrears (3,000 Shares × ₹2)	6,000	1,94,000

(4) **Called-up Capital :** Called-up Capital means such part of the Subscribed Capital, which has been called by the directors from shareholders for payment. For example, if the directors call at the rate of ₹60 per share on 12,000 shares of ₹100 each, ₹7,20,000 will be the called up Capital. The remaining amount of ₹40 per share will be uncalled Capital.

(5) **Paid-up Capital :** The term "**Paid-up**" refers to the amount received against the calls made on the shares. Usually the called-up Capital and the paid-up Capital are the same except that some shareholders may not have paid the amount of calls. Any unpaid amount is called 'Calls in arrear'. If a shareholder has paid ₹5 against the called-up amount of ₹8, then ₹5 is paid-up amount. Paid up Capital will be called up Capital less the amount of calls in arrear.

(6) **Reserve Capital :** As per Section 65 of the Companies Act, 2013, only an unlimited company having a share capital while converting into a limited company, may have reserve capital. In such a case, the company by a resolution may

- (*i*) increase the nominal amount of its share capital by increasing the nominal amount of each of its shares, and determine that no part of the increased capital shall be called up except in the event of winding up of the company; or
- (*ii*) provide that a specified portion of its uncalled share capital shall not be called except in the event of winding up of the company.

In such a case the increased capital in Case (*i*) or specified portion of uncalled capital in case (*ii*) becomes Reserve Capital. It is available only for the creditors on the winding up of the company.

Presentation of Share Capital in Company's Balance Sheet

As per **Schedule III** of Companies Act, 2013, Share Capital is to be disclosed in a Company's Balance Sheet in the following manner :

EXTRACT OF BALANCE SHEET OF................ *as at* ....

Particulars	*Note No.*	*Amount Current Year*	*Amount Previous Year*
I. EQUITY AND LIABILITIES :		₹	₹
Shareholder's Funds :			
(*a*) Share Capital*	(1)	....	
(*b*) Reserves and Surplus		....	
(*c*) Money received against share warrants		....	....

* As per Schedule III disclosure requirements pertaining to Share Capital are to be provided in notes to accounts.

Notes to Accounts :

		₹	₹
(1) **Share Capital**			
Authorised Capital* :			
.... Equity Shares of ₹....... each			
.... Preference Shares of ₹....... each			
Issued Capital :			
.... Equity Shares of ₹....... each			
.... Preference Shares of ₹....... each			
Subscribed Capital :			
Subscribed and Fully Paid Capital :			
.... Equity Shares of ₹....... each			
.... Preference Shares of ₹....... each	₹...........		
(Of the above shares............. Shares are allotted as fully paid-up pursuant to a contract without payments being received in cash)			
Subscribed but not fully paid Capital : ...... Shares of ₹....... each, ₹......... per share Called-up	₹..........		
Less : Calls in Arrears :			
(*i*) By Directors and Officers of the Company	₹..........		
(*ii*) By Others	₹..........		
Add : Forfeited shares	₹..........	....	....

* As per ISC Guidelines, Authorised/Issued Capital has to be shown in the notes to accounts even if it is not given in the question.

Capital Reserves : Capital reserves are those reserves which are created out of Capital profits. Capital profits are those profits which are not earned in the normal course of the business. These reserves cannot be utilised for the distribution of dividends. Following are the items that give rise to Capital profits and hence Capital reserves :

(I) Profit on sale of fixed assets.

(II) Profit on revaluation of fixed assets.

(III) Premium on issue of shares and debentures.

(IV) Profit on redemption of debentures.

(V) Profit earned by a company prior to its incorporation.

(VI) Profit on forfeiture and re-issue of shares.

Capital Reserves are shown on the liabilities side of the Balance Sheet under the head "Reserves and Surplus."

Distinction between Reserve Capital and Capital Reserves

Basis of Distinction	*Reserve Capital*	*Capital Reserve*
1. **Meaning and Creation**	It refers to that portion of increased nominal capital or uncalled share capital which shall not be called up, except in the event of winding up.	Capital Reserve is that reserve which is created out of Capital profits such as profit on sale of fixed assets, profit on revaluation of fixed assets, premium on issue of shares and debentures, profit on redemption of debentures etc. These profits are not earned in the normal course of business.
2. **Necessity**	It is not necessary to create Reserve Capital.	It is necessary to create Capital Reserve, in case of Capital profits.
3. **Resolution**	A resolution is required for its creation.	No resolution is required for the creation of Capital Reserves.
4. **Realised or not realised**	It refers to the amount which has not been received.	It refers to the amount which has already been received.
5. **Disclosure in Balance Sheet**	It is not shown in the Company's balance sheet.	It is shown as the first item under the head, 'Reserves and Surplus' on the equity and liabilities side of the balance sheet.
6. **Time when it can be used**	It can be used only at the time of winding up of the Company.	It can be used to write off Capital losses or to declare a share bonus any time during the life of the Company.

Distinction between Authorised Capital and Issued Capital

Basis of Distinction	*Authorised/Nominal or Registered Capital*	*Issued Capital*
1. **Meaning**	It is the maximum amount for which a Company is authorised to issue shares.	It is that part of the authorised capital which is offered to the public for subscription.
2. **Disclosure**	It is stated in the Memorandum of Association of the Company.	It is stated in the Articles of Association of the Company.
3. **Limit**	It is equal to or more than the issued capital.	It is equal to or less than the authorised capital.

Issue of Shares

Shares may be issued in any of the following ways :

(*i*) For Cash : By Public Subscription of shares

(*ii*) For Consideration other than Cash.

(*i*) Public Subscription of Shares

Following steps are to be taken by a Public Company for the issue of shares to public :

(1) To Issue Prospectus.

(2) To Receive Applications.

(3) To Make Allotments.

(4) To Make Calls.

(1) **To Issue Prospectus** : Prospectus is an invitation to the public to purchase its shares. It describes the profitability and soundness of the business of the Company to attract the investing public. It contains the following informations :

Name and address of the registered office of the Company, Names and addresses of the directors, Objects of the Company, risks involved in the issue, Consent from SEBI (Securities and Exchange Board of India), Authorised and Issued Capital of the company and the number of shares now offered for subscription, terms of present issue, dates of opening and closing of the issue etc.

(2) **To Receive Applications** : After reading the prospectus the public applies for shares in the Company on a prescribed form. Each application must accompany the application money which is mentioned in the prospectus, but it should not be less than 25% of the issue price of each share.

The amount of share application money must be deposited by the public in a Scheduled Bank. The name of the Company's Scheduled Bank is also mentioned in the prospectus.

(3) **To Make Allotment of Shares** : After the last date fixed for receipt of application money expires, the Bank sends all applications to the Company. The directors of the Company cannot proceed to allot shares unless **Minimum Subscription** mentioned in the prospectus has been received by the Company.

Minimum Subscription : Section 39 (1) of the Companies Act, 2013 provides that a Company cannot allot any securities of the Company to public unless the amount stated in the prospectus as the **minimum amount** has been subscribed and the sum payable on application for the amount so stated have been received by the Company by cheque or other instrument which has been paid. Minimum Subscription means the amount which, in the opinion of the Directors, is the minimum to be raised by the issue of shares so as to provide for the following requirements :

(*i*) For the payment of purchase price of any property purchased or agreed to be purchased;

(*ii*) For the payment of preliminary expenses, including underwriting commission and brokerage on issue of shares;

(*iii*) For the repayment of any moneys borrowed by the Company for the above purposes;

(*iv*) For Working Capital; and

(*v*) For any other expenditure required for the usual conduct of business operations.

The Companies Act, 2013 has not prescribed the minimum subscription. However, According to SEBI Guidelines minimum subscription has been fixed at 90% of the issued amount. As per Section 39(3), company has to get minimum subscription within 30 days from the date of the issue of the prospectus. If the company fails to receive the minimum subscription within the said period, the company cannot proceed with the allotment of shares and the entire application money must be returned within next 15 days. If there is a delay in refund of such amount by more than 15 days, the Company shall be liable to repay it with interest at the rate of 15% per annum for the delayed period.

Each allottee will be issued share certificates for eligible number of shares.

In case of oversubscription of shares, the allotment shall be on a proportionate basis according to the number of shares applied for.

For example, if a company issues a prospectus inviting applications for 1,00,000 shares and if applications are received for 4,00,000 shares, the issue has been over subscribed by 4 times. In such a case, an applicant in the category of 500 shares is entitled to the proportionate allotment of $\frac{500}{4} = 125$ shares.

As a result of over subscription, some applications may be rejected in full. Others may be partially accepted and still others may be accepted in full. Those who are allotted shares are sent 'Letters of Allotment' indicating the number of shares allotted and the amount now due on allotment. Those who are not allotted shares are sent *'Letters of Regret'* alongwith a cheque for the refund of application money.

(4) **To Make Calls :** The amounts paid on application and allotment are not calls but subsequent instalments, as and when demanded, are calls. A Company may demand the whole amount of a share on application in one instalment. If the whole of the amount of share is not paid on application and allotment, the unpaid amount may be called by the directors in one or more instalments. Each instalment is named as First Call, Second Call etc. Calls must be made strictly in accordance with the provisions of the Articles of Association. In the absence of the Articles of Association, the provisions of Table F of Schedule I of the Companies Act, 2013 shall apply. These provisions are :

1. The amount of one call shall not exceed 25% of the face value of the share.
2. All amount on shares should be fully called up within a period of 12 months from the date of allotment.
3. There must be an interval of atleast one month between the making of two calls.
4. Atleast 14 days notice must be given to the shareholders to pay the amount of call.
5. Calls must be made on a uniform basis on all the shares within the same class of shares.

A Call letter must specify the amount of the call, mode of remitting money, address to which call money is required to be sent and the last date for sending the money.

Preliminary Expenses

Expenses incurred on the formation of a Company are termed as 'Preliminary Expenses'. These include the following :

I. Expenses incurred on the preparation and printing of various documents needed for the registration of a Company.

II. Stamp duty and registration fees on these documents.

III. Duty payable on Authorised Capital.

IV. Cost of preliminary books.

V. In case the Company has been formed to purchase a running business, the fees charged by Accountant or Valuer valuing the assets and liabilities of that business.

> As per AS-26 Preliminary Expenses are to be written off in the year in which they are incurred. They should be written off first from Securities Premium Reserve Account and in its absence from General Reserve or from Surplus *i.e.*, balance in Statement of Profit & Loss under the head 'Reserve and Surplus'.

Entries on Issue of Shares for Cash

Entry on Receiving Applications :

(1) The application money must be deposited by the Company in a 'Scheduled Bank'. The following entry is made by the Company on receiving the applications :

Bank A/c Dr.
To Share Application A/c
(Application money received on .... shares at the rate of ₹......... per share)

Entries on Allotment :

(2) Application money is a part of the share capital of the Company, and as such, when the directors allot the shares, the share application money is transferred to Share Capital Account. For this the following journal entry is passed :

I. Share Application A/c Dr.
To Share Capital A/c
(Application money on allotted shares transferred to Share Capital A/c)

II. Sometimes, the directors do not allot any shares to some of the applicants. The application money of such applicants is returned to them. The entry will be :

Share Application A/c Dr.
To Bank A/c
(Application money returned on un-allotted shares)

(3) Those applicants who are allotted shares are sent letters of allotment in which the number of shares allotted and the amount due on allotment is mentioned. As soon

as the allotment letters are issued, the allotment money becomes due and becomes a part of Share Capital. The entry required is :

Share Allotment A/c Dr.
To Share Capital A/c
(Amount due on allotment on .... shares at the rate of ₹........ per share)

(4) On receipt of Allotment Money :

Bank A/c Dr.
To Share Allotment A/c
(Amount received on allotment on.......... shares at the rate of ₹.......... per share)

Entries on First Call :

(5) When Shareholders are informed to pay the First Call :

Share First Call A/c Dr.
To Share Capital A/c
(First call due on .... shares at the rate of ₹.................... per share)

(6) On receipt of First Call Money :

Bank A/c Dr.
To Share First Call A/c
(First Call money received on .... shares at the rate of ₹........... per share)

Entries on Second Call :

(7) When shareholders are informed to pay the Second Call :

Share Second Call A/c Dr.
To Share Capital A/c
(Second Call due on .... shares at the rate of ₹........... per share)

(8) On receipt of Second Call Money :

Bank A/c Dr.
To Share Second Call A/c
(Second Call money received on .... shares at the rate of ₹.......... per share)

Similarly, entries for other calls may be prepared.

Issue of Shares at Par

Shares are issued at par when they are issued at a price equal to the face value. For example, if a share of ₹10 is issued at ₹10, it is said that the share has been issued at par.

ILLUSTRATION 4.

Pawan Ltd. invited applications for 30,000 shares of ₹10 each. Payments were to be made as follows — ₹3 on Application; ₹3 on Allotment; ₹2 on First call and ₹2 on Final call.

All the shares were applied. You are required to prepare Journal Entries, Ledger Accounts and show how the share capital will be presented in the Opening Balance Sheet of the company assuming that all sums due on Allotment and Calls have been received. Share Issue expenses amounted to ₹8,000. 4,000 fully paid shares were also issued to Promoters for their services.

SOLUTION : JOURNAL ENTRIES

Date	*Particulars*	*L.F.*	*Dr.* (₹)	*Cr.* (₹)
	On date of Receipt Bank A/c Dr. To Equity Share Application A/c (Money received on application for 30,000 shares @ ₹3 per share)		90,000	90,000
	On date of Allotment Equity Share Application A/c Dr. To Equity Share Capital A/c (Transfer of application money to Share Capital A/c)		90,000	90,000
	On date of Allotment Equity Share Allotment A/c Dr. To Equity Share Capital A/c (Allotment money due on 30,000 shares @ ₹3 per share)		90,000	90,000
	On date of Receipt Bank A/c Dr. To Equity Share Allotment A/c (Allotment money received)		90,000	90,000
	On date of Call Equity Share First Call A/c Dr. To Equity Share Capital A/c (First call due on 30,000 shares @ ₹2 per share)		60,000	60,000
	On date of Receipt Bank A/c Dr. To Equity Share First Call A/c (Amount received on first call)		60,000	60,000
	On date of Call Equity Share Final Call A/c Dr. To Equity Share Capital A/c (Final call due on 30,000 shares @ ₹2 per share)		60,000	60,000
	On date of Receipt Bank A/c Dr. To Equity Share Final Call A/c (Amount received on final call)		60,000	60,000
	Share Issue Expenses A/c Dr. To Bank A/c (Expenses incurred on issue of shares)		8,000	8,000
	Incorporation Costs A/c Dr. To Equity Share Capital A/c (Fully paid shares issued to promoters for their services)		40,000	40,000
	Statement of Profit & Loss Dr. To Share Issue Expenses A/c To Incorporation Costs A/c (Share Issue Expenses and Incorporation costs written off)		48,000	 8,000 40,000

Notes : (1) The entry for receiving Share Application money is passed first and the entry for transferring the application money to Share Capital A/c is passed thereafter. This is done, because Cash is received first and allotment is made afterwards.

(2) In case of Allotment, First Call and Second Call, the entry for transferring the same to Share Capital A/c is made first when the resolution is passed and the entry for receiving money from shareholders is made afterwards as money from shareholders is received only afterwards.

(3) In case nothing is mentioned regarding the class of shares issued, they are always treated as equity shares.

(4) In actual practice all cash transactions are passed through the Cash Book. Hence, there will be no journal entries relating to cash and there will not be a Bank Account in the Ledger.

Ledger Accounts

Dr. BANK ACCOUNT Cr.

Particulars	₹	*Particulars*	₹
To Equity Share Application A/c	90,000	By Share Issue Expenses A/c	8,000
To Equity Share Allotment A/c	90,000	By Balance c/d	2,92,000
To Equity Share First Call A/c	60,000		
To Equity Share Final Call A/c	60,000		
	3,00,000		3,00,000

Dr. EQUITY SHARE APPLICATION ACCOUNT Cr.

Particulars	₹	*Particulars*	₹
To Equity Share Capital A/c	90,000	By Bank A/c	90,000
	90,000		90,000

Dr. EQUITY SHARE ALLOTMENT ACCOUNT Cr.

Particulars	₹	*Particulars*	₹
To Equity Share Capital A/c	90,000	By Bank A/c	90,000
	90,000		90,000

Dr. EQUITY SHARE FIRST CALL ACCOUNT Cr.

Particulars	₹	*Particulars*	₹
To Equity Share Capital A/c	60,000	By Bank A/c	60,000
	60,000		60,000

Dr. EQUITY SHARE FINAL CALL ACCOUNT Cr.

Particulars	₹	*Particulars*	₹
To Equity Share Capital A/c	60,000	By Bank A/c	60,000
	60,000		60,000

Dr. EQUITY SHARE CAPITAL ACCOUNT Cr.

Particulars	₹	*Particulars*	₹
To Balance c/d	3,40,000	By Equity Share Application A/c	90,000
		By Equity Share Allotment A/c	90,000

		By Equity Share First Call A/c	60,000
		By Equity Share Final Call A/c	60,000
		By Incorporation Costs A/c	40,000
	3,40,000		3,40,000

Dr. SHARE ISSUE EXPENSES ACCOUNT Cr.

Particulars	₹	*Particulars*	₹
To Bank A/c	8,000	By Statement of Profit & Loss	8,000
	8,000		8,000

Dr. INCORPORATION COSTS ACCOUNT Cr.

Particulars	₹	*Particulars*	₹
To Equity Share Capital A/c	40,000	By Statement of Profit & Loss	40,000
	40,000		40,000

EXTRACT OF BALANCE SHEET OF PAWAN LTD.

as at ....

Particulars	*Note No.*	*Current year*	*Previous year*
I. EQUITY AND LIABILITIES :		₹	₹
Shareholder's Funds :			
(*a*) Share Capital	1	3,40,000	

Notes to Accounts :

	₹	₹
(1) **Share Capital**		
Authorised* :		
.........Shares of ₹............... each	....	
Issued, subscribed and fully paid-up :		
34,000 Equity Shares of ₹10 each (of the above shares, 4,000 shares are allotted as fully paid-up pursuant to contracts without payments being received in cash)	3,40,000	

*As per ISC Guidelines, even if authorised/issued capital is not given in the question, it has to be shown in the notes to accounts.

Issue of Shares at Premium

When a Company issues a share at a price which is above its face value, it is said to be issued at premium. For example, if a share of the face value of ₹10 is issued at ₹12, ₹2 will be the premium on the share. There is no legal restriction on issue of shares at a premium.

The premium on issue of shares is a Capital profit and not a revenue profit and as such, must be credited to a separate account called 'Securities Premium Reserve Account'. It must be shown separately in the Balance Sheet on the equity & liabilities side under the head 'Reserves and Surplus'.

Securities Premium A/c Versus Securities Premium Reserve A/c

As per Section 52 (1) of the Companies Act, 2013 the amount of premium received should be credited to 'Securities Premium A/c' whereas Schedule III of the Companies Act, 2013 has given the head 'Securities Premium Reserve'. Students may use either of the two terms while making the journal entries.

Under section 52 (2) of the Companies Act, 2013, the amount of securities premium reserve may be used only for the following purposes :

(1) In writing off the preliminary expenses of the Company;

(2) For writing off the expenses, Commission or discount allowed on issue of shares or debentures of the Company;

(3) For issuing fully paid bonus shares to the shareholders of the Company;

(4) For providing for the premium payable on redemption of redeemable preference shares or debentures of the Company.

(5) For Buy back of its own shares and other securities as per section 68.

Accounting Entries for the Amount of Securities Premium :

The amount of securities premium may be charged by the Company on application or on allotment or even with the calls. Following entries will be passed, if the amount of premium is received alongwith application money :

I. Bank A/c Dr.
To Share Application A/c
(Application money received including premium)

II. Share Application A/c Dr.
To Share Capital A/c
To Securities Premium Reserve A/c
(Application money transferred to Share Capital A/c and Securities Premium Reserve A/c)

If the amount of securities premium is received alongwith allotment money, the following entries will be passed :

I. Share Allotment A/c Dr.
To Share Capital A/c
To Securities Premium Reserve A/c
(Allotment money due, including securities premium)

II. When allotment money is received :

Bank A/c Dr.
To Share Allotment A/c
(Allotment money received, including securities premium)

Normally, it is mentioned in the question as to when the securities premium is receivable, *i.e.*, either it is payable on application or on allotment or on calls. **In the absence of any information, it is assumed that the securities premium is due alongwith allotment money.**

ILLUSTRATION 5.

Spencer Paints Ltd. was registered with an authorised capital of ₹50,00,000 divided in 5,00,000 equity shares of ₹10 each. Company issued 2,00,000 equity shares at a premium of ₹3 per share, payable as follows : ₹4 on Application; ₹5 on Allotment (including premium); ₹2 on First Call and ₹2 on Second and Final Call.

All shares were subscribed and all the money was duly received. Share issue expenses amounted to ₹75,000 which were fully written off against Securities Premium.

Prepare necessary Journal Entries, Bank Account and Opening Balance Sheet.

SOLUTION : JOURNAL

Date	*Particulars*	*L.F.*	*Dr.*	*Cr.*
			₹	₹
	Bank A/c Dr. To Equity Share Application A/c (Money received on application)		8,00,000	 8,00,000
	Equity Share Application A/c Dr. To Equity Share Capital A/c (Application money transferred to Share Capital A/c)		8,00,000	 8,00,000
	Equity Share Allotment A/c Dr. To Equity Share Capital A/c To Securities Premium Reserve A/c (Allotment, including premium due)		10,00,000	 4,00,000 6,00,000
	Bank A/c Dr. To Equity Share Allotment A/c (Allotment money received, including premium)		10,00,000	 10,00,000
	Equity Share First Call A/c Dr. To Equity Share Capital A/c (Money due on first call)		4,00,000	 4,00,000
	Bank A/c Dr. To Equity Share First Call A/c (Money received on first call)		4,00,000	 4,00,000
	Equity Share Second & Final Call A/c Dr. To Equity Share Capital A/c (Money due on second & final call)		4,00,000	 4,00,000
	Bank A/c Dr. To Equity Share Second & Final Call A/c (Money received on second & final call)		4,00,000	 4,00,000
	Share Issue Expenses A/c Dr. To Bank A/c (Expenses incurred on issue of shares)		75,000	 75,000
	Securities Premium Reserve A/c Dr. To Share Issue Expenses A/c (Share issue expenses written off against Securities Premium Reserve A/c)		75,000	 75,000

Dr. BANK ACCOUNT Cr.

Particulars	₹	*Particulars*	₹
To Equity Share Application A/c	8,00,000	By Share Issue Expenses A/c	75,000
To Equity Share Allotment A/c	10,00,000	By Balance c/d	25,25,000
To Equity Share First Call A/c	4,00,000		
To Equity Share Second & Final Call A/c	4,00,000		
	26,00,000		26,00,000

BALANCE SHEET OF SPENCER PAINTS LTD.

as at..... ....

Particulars	*Note No.*	*Current year*	*Previous year*
I. EQUITY AND LIABILITIES :		₹	₹
Shareholder's Funds :			
(*a*) Share Capital	1	20,00,000	
(*b*) Reserve and Surplus	2	5,25,000	
		25,25,000	
II. ASSETS :			
Current Assets :			
Cash and Bank Balance	3	25,25,000	

Notes to Accounts :

	₹	₹
(1) **Share Capital :**		
Authorised :		
5,00,000 Equity Shares of ₹10 each	50,00,000	
Issued, Subscribed & Fully Paid Capital :		
2,00,000 Equity Shares of ₹10 each	20,00,000	
(2) **Reserve and Surplus :**		
Securities Premium Reserve	5,25,000	
(3) **Cash and Bank Balance :**		
Cash at Bank	25,25,000	

Issue of Shares at Discount

When a share is issued at a price which is less than its face value, it is said that it has been issued at a discount. For example, if a share of the nominal value of ₹100 is issued at ₹95, it is said to have been issued at a discount of 5%.

Prohibition on issue of shares at a discount

As per Section 53 of Companies Act 2013, Companies would no longer be permitted to issue shares at a discount. The only shares that could be issued at a discount are sweat equity wherein shares are issued to employees or directors in lieu of their services under Section 54 of 2013 Act.

Under-subscription of Shares

Sometimes, number of shares applied for by the public is less than the number of shares offered by the Company. Such an issue is said to be under-subscribed. In such a case the accounting entries are made on the basis of the number of shares applied for.

ILLUSTRATION 6.

Shiva Ltd. issued 20,000 shares of ₹10 each at a premium of 10%. Payments were to be made as — on Application ₹5 (including premium); on Allotment ₹4 and on First and Final Call ₹2.

Applications were received for 18,000 shares and all were accepted. All money was duly received.

Pass necessary entries in the Books of the Company and also show the Balance Sheet of the Company.

SOLUTION :

JOURNAL

Date	*Particulars*		*L.F.*	*Dr.*	*Cr.*
				₹	₹
	Bank A/c	Dr.		90,000	
	To Share Application A/c				90,000
	(Money received on application for 18,000 shares @ ₹5 per share including premium)				
	Share Application A/c	Dr.		90,000	
	To Share Capital A/c				72,000
	To Securities Premium Reserve A/c				18,000
	(Transfer of application money to share capital A/c)				
	Share Allotment A/c	Dr.		72,000	
	To Share Capital A/c				72,000
	(Amount due on allotment, excluding discount)				
	Bank A/c	Dr.		72,000	
	To Share Allotment A/c				72,000
	(Allotment money received)				
	Share First and Final call A/c	Dr.		36,000	
	To Share Capital A/c				36,000
	(Share first and final call due)				
	Bank A/c	Dr.		36,000	
	To Share First and Final call A/c				36,000
	(Share first and final call money received)				

BALANCE SHEET OF SHIVA LTD.

as at..............

Particulars	*Note No.*	*Current year*	*Previous year*
I. EQUITY AND LIABILITIES :		₹	₹
Shareholder's Funds :			
(*a*) Share Capital	1	1,80,000	

(*b*) Reserve and Surplus	2	18,000	
		1,98,000	
II. ASSETS :			
Current Assets :			
Cash and Bank Balance	3	1,98,000	

Notes to Accounts :

	₹	₹
(1) **Share Capital :**		
Authorized Capital		
.... Shares of ₹10 each	....	
Issued Capital : 20,000 Shares of ₹10 each	2,00,000	
Subscribed and fully paid Capital: 18,000 Shares of ₹10 each fully paid	1,80,000	
(2) **Reserve and Surplus :** Securities Premium Reserve	18,000	
(3) **Cash and Bank Balance :** Cash at Bank	1,98,000	

(*ii*) Issue of Shares for Consideration other than Cash

It is not necessary to issue the shares only for cash. A Company may issue fully paid shares for consideration other than cash, in the following circumstances :

(1) Issue of Shares to Promoters :

Promoters of a Company may be issued shares in the Company for the services rendered by them. The entry will be :

Incorporation Costs or Formation Exp. A/c Dr.
To Share Capital A/c
(Shares issued to Promoters)

(2) Issue of Shares to Underwriters :

Underwriting is an agreement entered into before the issue is brought before the public that if the shares or debentures are not taken up by the public in full, underwriters will have to take up and pay for such part of the shares or debentures which the public has not applied for. The persons or institutions who or which guarantee or undertake the issue are known as underwriters. For the guarantee or the service rendered by them, they charge an agreed commission known as 'Underwriting Commission'. The Company may allot shares to underwriters to pay their commission. When the shares are allotted to discharge underwriting commission, the following entries will be passed:

(*i*) On making the commission payable to underwriters :

Underwriting Commission A/c Dr.
To Underwriters A/c
(Underwriting Commission due)

(*ii*) On payment of commission in the form of shares :
Underwriters A/c Dr.
To Share Capital A/c
(Allotment of Shares to Underwriters for the commission due to them)

(3) Issue of Shares to Vendors :

Sometimes, a Company purchases some assets and instead of making the payment to the vendors in the form of Cash, it issues fully paid shares to the vendors. Following journal entries are made for this purpose :

I. When assets are purchased from vendors :

Sundry Assets A/c Dr.
To Vendor's A/c

II. When shares are issued to vendors :

Vendor's A/c Dr.
To Share Capital A/c

ILLUSTRATION 7.

X Ltd. purchased the business of *Y* Ltd. for ₹9,00,000 payable in fully paid shares of ₹10 each. What entries will be made in the books of *X* Ltd. if such issue is : (*i*) at par, and (*ii*) at a premium of 25%.

SOLUTION : **In the Books of *X* LTD.**

Date	*Particulars*		*L.F.*	*Dr.*	*Cr.*
				₹	₹
	Sundry Assets A/c	Dr.		9,00,000	
	To *Y* Ltd.				9,00,000
	(Purchase of business of *Y* Ltd.)				
(*i*)	*When shares are issued at par :*				
	Y Ltd.	Dr.		9,00,000	
	To Share Capital A/c				9,00,000
	(Issue of 90,000 fully paid shares of ₹10 each to the Vendors)				
(*ii*)	*When shares are issued at premium :*				
	Y Ltd.	Dr.		9,00,000	
	To Share Capital A/c				7,20,000
	To Securities Premium Reserve A/c				1,80,000
	(Issue of 72,000 fully paid shares of ₹10 each at a premium of 25% calculated as follows : $\frac{9,00,000}{12.50}$ = 72,000 Shares)				

ILLUSTRATION 8.

Tulip Ltd. issued 50,000 shares of ₹10 each credited as fully paid to the promoters for their services. It also issued 30,000 shares of ₹10 each credited as fully paid to the underwriters for their commission. Give journal entries.

SOLUTION : **Journal of Tulip Ltd.**

Date	Particulars		L.F.	Dr.	Cr.
				₹	₹
	Incorporation Costs A/c	Dr.		5,00,000	
	To Share Capital A/c				5,00,000
	(Issue of 50,000 shares of ₹10 each to promoters)				
	Underwriting Commission A/c	Dr.		3,00,000	
	To Underwriter's A/c				3,00,000
	(Underwriting Commision due)				
	Underwriter's A/c	Dr.		3,00,000	
	To Share Capital A/c				3,00,000
	(Issue of 30,000 shares of ₹10 each to underwriters)				

ILLUSTRATION 9.

Prince Ltd. purchased a running business from Queens Ltd. for a sum of ₹30,00,000 payable 40% by a cheque and the balance by the issue of fully paid equity shares of ₹100 each at a premium of 20%. The assets and liabilities consisted of the following :

	Book Value	Agreed Value
	₹	₹
Building	10,00,000	16,00,000
Plant & Machinery	8,00,000	5,00,000
Stock	4,00,000	120%
Sundry Debtors	3,00,000	Subject to Provision for Doubtful Debts @ 5%
Cash & Bank	1,20,000	1,20,000
Sundry Creditors	2,00,000	1,85,000

Pass the necessary Journal entries in the books of Prince Ltd.

SOLUTION : JOURNAL OF PRINCE LTD.

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
	Building A/c	Dr.		16,00,000	
	Plant and Machinery A/c	Dr.		5,00,000	
	Stock A/c	Dr.		4,80,000	
	Sundry Debtors A/c	Dr.		3,00,000	
	Cash & Bank A/c	Dr.		1,20,000	
	Goodwill A/c (Balancing Figure)	Dr.		2,00,000	
	To Provision for Doubtful Debts A/c				15,000
	To Sundry Creditors A/c				1,85,000
	To Queens Ltd.				30,00,000
	(Purchase of business from Queens Ltd.)				
	Queens Ltd.	Dr.		12,00,000	
	To Bank A/c				12,00,000
	(40% payment made by cheque)				

	Queens Ltd. Dr. To Equity Share Capital A/c To Securities Premium Reserve A/c (Balance payment made by issue of 15,000 equity shares of ₹100 each at 20% premium)		18,00,000	 15,00,000 3,00,000

Working Note :

Number of Equity Shares to be issued : $\frac{₹18,00,000}{120}$ = 15,000 Shares.

ILLUSTRATION 10.

Sico Ltd. took over the assets of ₹4,80,000 and liabilities of ₹80,000 of Mittal Ltd. for a consideration of ₹3,20,000. ₹20,000 were paid by an acceptance in favour of Mittal Ltd. payable after 3 months and the balance by issue of fully paid 8% Preference Shares of ₹100 each at a premium of 50%. Pass the necessary journal entries for the above transactions in the books of Sico Ltd.

SOLUTION :

Books of Sico Ltd.

JOURNAL

Date	*Particulars*	*L.F.*	*Dr. Amount*	*Cr. Amount*
			₹	₹
(*i*)	Sundry Assets A/c Dr.		4,80,000	
	To Liabilities A/c			80,000
	To Mittal Ltd.			3,20,000
	To Capital Reserve A/c (Balancing figure)			80,000
	(Assets and Liabilities of Mittal Ltd. taken over)			
(*ii*)	Mittal Ltd. Dr.		3,20,000	
	To Bills Payable A/c			20,000
	To 8% Preference Share Capital A/c			2,00,000
	To Securities Premium Reserve A/c			1,00,000
	(Bills payable accepted and 2,000 preference shares issued at a premium of 50%)			

Working Note :

	₹
Total Amount payable	3,20,000
Less : B/P issued	20,000
	3,00,000

Number of Pref. Shares issued = $\frac{3,00,000}{150}$ = 2,000

Calls in Arrear

It often happens that some shareholders fail to pay the amount of allotment or call when it becomes due. This is known as calls in arrears. There are two methods to deal with calls in arrears :

(*i*) **Without Opening Calls-in-Arrear Account :** Under this method, there is no need to open calls-in-arrear account. In such a case the actual amount received from the shareholders is credited to the call account and the call account will show a debit balance equal to the unpaid amount of the call. On a subsequent date, when the unpaid amount is received, Bank Account is debited and the relevant Call A/c is credited.

(*ii*) **By Opening Calls in Arrear Account** : Under this method, 'Calls in Arrear A/c' is opened and this account is debited when some amount of allotment or calls is not received. On a later date, when the arrear amount is received, Bank Account is debited and the Calls in Arrear A/c is credited.

Suppose, *X* Ltd. made a first call of ₹2 per share on its 10,000 shares. One shareholder holding 500 shares did not pay the first call but when the company made final call of ₹3 per share, he paid all his arrears.

In this case we can adop any of the two methods mentioned above :

Without Opening Calls in Arrear A/c			By Opening Calls in Arrear A/c		
(*i*) **On making first call due :**			**On making first call due :**		
Share First Call A/c	Dr. 20,000		Share First Call A/c	Dr. 20,000	
To Share Capital A/c		20,000	To Share Capital A/c		20,000
(*ii*) **On receipt of first call :**			**On receipt of first call :**		
Bank A/c	Dr. 19,000		Bank A/c	Dr. 19,000	
To Share First Call A/c		19,000	Calls in Arrear A/c	Dr. 1,000	
			To Share First Call A/c		20,000
(*iii*) **On making final call due :**			**On making final call due :**		
Share Final Call A/c	Dr. 30,000		Share Final Call A/c	Dr. 30,000	
To Share Capital A/c		30,000	To Share Capital A/c		30,000
(*iv*) **On receipt of final call :**			**On receipt of final call :**		
Bank A/c	Dr. 31,000		Bank A/c	Dr. 31,000	
To Share Final Call A/c		30,000	To Share Final Call A/c		30,000
To Share First Call A/c		1,000	To Calls in Arrear A/c		1,000

Note : Whether the calls in Arrear A/c is opened or not, the amount of calls in arrear is shown as a deduction from the amount of subscribed but not fully paid capital on the equity & liabilities side of the Balance Sheet. This account is closed when the amount of arrear is received or the relevant shares are forfeited.

Interest on Calls in Arrear

The Company is authorised to charge interest on Calls in arrears at a specified rate mentioned in its articles, from the due date to the date of actual payment. But if the articles are silent, Table F of Schedule I of the Companies Act, 2013 shall be applicable, according to which interest shall be charged at a rate not exceeding 10% p.a. However, the directors have the right to waive the payment of such interest wholly or in part.

The journal entries for recording interest on calls in arrear are as follows :

(*i*) On making due the interest on Calls in Arrear :

Sundry Members A/c Dr.

To Interest on Calls in Arrear A/c

(*ii*) On receipt of interest on Calls in Arrear :

Bank A/c Dr.

To Sundry Members A/c

(*iii*) On transfer of interest on calls in arrear to Profit & Loss A/c at the end of accounting period :

Interest on Calls-in-Arrear A/c Dr.

To Statement of Profit and Loss

Use of Cash Book

A Cash Book is prepared to record cash transactions. If a student is asked to prepare a Cash Book in the question, entries for cash transactions must be recorded in the Cash Book and those transactions which are not related with Cash are recorded in journal.

ILLUSTRATION 11.

Chandra Ltd. issued 15,000 Preference shares of ₹100 each at a premium of 5%. Payments were to be made as — ₹25 on Application; ₹45 on Allotment and ₹35 on First and Final Call.

The applications for 14,000 shares were received and all were accepted. All the money was duly received except the first and final call on 200 shares.

Give the necessary Journal Entries and prepare Cash Book of the Company. Also prepare call in Arrears Account and give the Opening Balance Sheet of the Company.

SOLUTION :

Dr. CASH BOOK (Bank Column) Cr.

Particulars	₹	*Particulars*	₹
To Preference Share Application A/c	3,50,000	By Balance c/d	14,63,000
To Preference Share Allotment A/c	6,30,000		
To Preference Share First & Final Call A/c	4,83,000		
	14,63,000		14,63,000

JOURNAL

Date	*Particulars*	*L.F.*	*Dr.*	*Cr.*
			₹	₹
	Preference Share Application A/c Dr.		3,50,000	
	To Preference Share Capital A/c			3,50,000
	(Application money transferred to capital A/c)			
	Preference Share Allotment A/c Dr.		6,30,000	
	To Preference Share Capital A/c			5,60,000
	To Securities Premium Reserve A/c*			70,000
	(Allotment due and ₹5 per share credited to Securities Premium Reserve A/c)			

	Preference Share First & Final Call A/c Dr.		4,90,000	
	To Preference Share Capital A/c			4,90,000
	(Amount due on first & final call A/c)			
	Calls in Arrears A/c Dr.		7,000	
	To Preference Share First & Final Call A/c			7,000
	(First and final call @ ₹35 per share unpaid on 200 shares)			

*It will be assumed that Securities Premium Reserve is due along with allotment.

Dr. CALLS-IN-ARREARS ACCOUNT Cr.

Date	*Particulars*	*J.F.*	₹	*Date*	*Particulars*	*J.F.*	₹
	To Preference Share First and Final Call A/c		7,000		By Balance c/d		7,000
			7,000				7,000

BALANCE SHEET OF CHANDRA LTD. *as at* ....

Particulars	*Note No.*	*Current year*	*Previous year*
I. EQUITY AND LIABILITIES :		₹	₹
Shareholder's Funds :			
(*a*) Share Capital	1	13,93,000	
(*b*) Reserve and Surplus	2	70,000	
		14,63,000	
II. ASSETS :			
Cash and Bank Balance	3	14,63,000	

Notes to Accounts :

			₹	₹
(1) **Share Capital**				
Authorised :				
.... Shares of ₹......... each			....	
Issued :				
15,000 Preference Shares of ₹100 each			15,00,000	
Subscribed and Fully Paid Capital :				
13,800 Preference Shares of ₹100 each		13,80,000		
Subscribed but not Fully Paid Capital :				
200 Preference Shares of ₹100 each	20,000			
Less : Calls in Arrear	7,000	13,000	13,93,000	
(2) **Reserve and Surplus :**				
Securities Premium Reserve			70,000	
(3) **Cash and Bank Balance :**				
Cash at Bank			14,63,000	

ILLUSTRATION 12.

Akruti Ltd. issued 2,00,000 Equity Shares of ₹10 each payable as follows :

₹3 on Application
₹3 on Allotment
₹2 on First Call (After 2 months)
₹2 on Final Call (After 3 months)

All the shares were subscribed. The Company allotted the shares and made the calls. The moneys due were received on due dates except on 4,000 shares allotted to Era who did not pay the allotment money and first call money on due dates but paid the due amount at the time of final call along with interest @10% p.a.

Pass Journal entries and show Calls-in-Arrears Account, Equity Share Allotment Account and Equity Share First Call Account.

SOLUTION :

JOURNAL OF AKRUTI LTD.

Date	*Particulars*		*L.F.*	*Dr.*	*Cr.*
				₹	₹
	Bank A/c	Dr.		6,00,000	
	To Equity Share Application A/c				6,00,000
	(Application money received)				
	Equity Share Application A/c	Dr.		6,00,000	
	To Equity Share Capital A/c				6,00,000
	(Application money transferred to Equity Share Capital Account)				
	Equity Share Allotment A/c	Dr.		6,00,000	
	To Equity Share Capital A/c				6,00,000
	(Allotment money due)				
	Bank A/c	Dr.		5,88,000	
	Calls-in-Arrears A/c	Dr.		12,000	
	To Equity Share Allotment A/c				6,00,000
	(Allotment money received except on 4,000 shares allotted to Era)				
	Equity Share First Call A/c	Dr.		4,00,000	
	To Equity Share Capital A/c				4,00,000
	(Share first call money due)				
	Bank A/c	Dr.		3,92,000	
	Calls-in-Arrears A/c	Dr.		8,000	
	To Equity Share First Call A/c				4,00,000
	(First call received except on 4,000 Shares allotted to Era)				
	Equity Share Second and Final Call A/c	Dr.		4,00,000	
	To Equity Share Capital A/c				4,00,000
	(Share second and final call money due)				
	Bank A/c	Dr.		4,20,700	
	To Equity Share Second and Final Call A/c				4,00,000
	To Calls-in-Arrears A/c				20,000
	To Interest on Calls-in-Arrears A/c				700
	(Share second and final call money received along with Calls-in-Arrears and interest)				

	Interest on Calls-in-Arrears A/c Dr.		700	
	To Statement of Profit and Loss			700
	(Interest on calls in arrears transferred)			

Dr. CALLS-IN-ARREARS ACCOUNT Cr.

Date	Particulars	J.F.	₹	Date	Particulars	J.F.	₹
	To Equity Share Allotment A/c		12,000		By Bank A/c		20,000
	To Equity Share First Call A/c		8,000				
			20,000				20,000

Dr. EQUITY SHARE ALLOTMENT ACCOUNT Cr.

Date	Particulars	J.F.	₹	Date	Particulars	J.F.	₹
	To Equity Share Capital A/c		6,00,000		By Bank A/c		5,88,000
					By Calls-in-Arrears A/c		12,000
			6,00,000				6,00,000

Dr. EQUITY SHARE FIRST CALL ACCOUNT Cr.

Date	Particulars	J.F.	₹	Date	Particulars	J.F.	₹
	To Equity Share Capital A/c		4,00,000		By Bank A/c		3,92,000
					By Calls-in-Arrears A/c		8,000
			4,00,000				4,00,000

Working Note :

Calculation of Interest on Calls in Arrears :

		₹
On ₹12,000 for 5 months :	$12{,}000 \times \frac{10}{100} \times \frac{5}{12} =$	500
On ₹ 8,000 for 3 months :	$8{,}000 \times \frac{10}{100} \times \frac{3}{12} =$	200
		700

CASE BASED MCQs — 1

Kaveri Ltd. was registered with an authorised capital of 40,000 equity shares of ₹100 each. It offered 30,000 equity shares to the public at a premium of ₹40 per share. The amount per share was payable as ₹30 on application; ₹70 (including premium) on allotment; and the balance on first and final call. 28,000 shares were subscribed by the public. All calls were made. A shareholder holding 1,000 shares failed to pay the allotment and first and final call money.

(*a*) Issued Capital will be :

(*i*) ₹27,30,000 (*ii*) ₹30,00,000

(*iii*) ₹42,00,000 (*iv*) ₹28,00,000

(*b*) Subscribed Capital will be :

(*i*) ₹27,00,000 (*ii*) ₹28,30,000
(*iii*) ₹28,00,000 (*iv*) ₹27,30,000

(*c*) Subscribed and Fully Paid Capital will be :

(*i*) ₹28,00,000 (*ii*) ₹28,30,000
(*iii*) ₹27,00,000 (*iv*) ₹27,30,000

(*d*) Subscribed but not Fully Paid Capital will be :

(*i*) ₹ 70,000 (*ii*) ₹ 30,000
(*iii*) ₹27,30,000 (*iv*) ₹1,00,000

(*e*) Balance of Securities Premium Reserve shown in Balance Sheet will be :

(*i*) ₹12,00,000 (*ii*) ₹10,80,000
(*iii*) ₹11,60,000 (*iv*) ₹11,20,000

Calls Paid-in-Advance

A shareholder may sometimes pay a part, or whole, of the amount not yet called upon his shares in order to save himself the trouble of paying different calls at different times. Thus the amount of future calls is received in advance by the Company. According to Section 50 of the Companies Act, 2013 such amount of Calls in advance can be accepted by the Company only when it is so authorised by its Articles of Association.

When the amount of Calls-in-Advance is received, it is credited to a newly opened account 'Calls in Advance A/c'. The entry will be :

Bank A/c Dr.
To Calls in Advance A/c
(Call received in Advance)

Calls in Advance A/c is shown on the equity & liabilities side of Balance Sheet under the main head "Current Liabilities" and sub-head 'Other Current Liabilities'.

In future, when the call is made by the directors, the following entries will be passed :

I. Share Call A/c Dr.
To Share Capital A/c
(When the amount becomes due on call on all shares including those on which call has been received in advance)

II. Bank A/c Dr. (With the amount actually received)
Calls in Advance A/c Dr. (With the amount of the Call received in advance)
To Share Call A/c
(Calls in Advance adjusted)

Interest on Calls in Advance :

The amount received as Calls in advance is a debt of the Company. It is liable to pay interest on Calls in advance from the date of receipt till the date when the Call is due for payment. Generally, the Articles of the Company specify the rate at which interest is payable. However, if the articles do not contain such rate, Table F of Schedule I of the Companies Act, 2013 shall be applicable which leaves the matter to the Board of Directors subject to a maximum rate of 12% p.a. It is to be noted that interest on Calls in Advance is a charge against the profits of the Company. As such, the interest on Calls in Advance is payable even if there are no profits. No Dividend is payable on Calls in advance since the amount of Calls in advance is not a part of share capital.

The journal entries for recording interest on calls in advance are as follows :

(*i*) On making due the interest on Calls in advance :

Interest on Calls in Advance A/c	Dr.
To Sundry Members A/c	

(*ii*) On payment of interest on Calls in advance :

Sundry Members A/c	Dr.
To Bank A/c	

(*iii*) On transfer of interest on calls in advance to Profit & Loss A/c at the end of accounting period :

Statement of Profit and Loss	Dr.
To Interest on Calls in Advance A/c	

Note : If rate of interest on Calls in Advance is not mentioned in the question, it will be 12% p.a.

ILLUSTRATION 13.

Raman Ltd. issued 20,000 shares of ₹10 each at par payable as follows :

₹2.50 on application payable on 1st May, 2021;

₹2.50 on allotment payable on 1st July, 2021;

₹2 on first call payable on 1st October, 2021;

Balance on second call payable on 1st February, 2022.

All these shares were subscribed and amounts received.

Shareholer *A* who had been allotted 200 shares, paid the amount of the first and second calls with allotment. Another shareholder *B* holding 100 shares did not pay the final call till the date of the Balance Sheet.

According to the Articles of Association of the company, interest @ 4% p.a. is payable by the company on any Calls-in-Advance. The interest was paid by the company to the shareholder on 1st February, 2022. Pass necessary Journal entries (including interest) in the books of the Company. Books are closed on 31st March every year.

SOLUTION :

In the Books of Raman Ltd.

JOURNAL

Date	*Particulars*		*L.F.*	*Dr.*	*Cr.*
2021				₹	₹
May 1	Bank A/c	Dr.		50,000	
	To Share Application A/c				50,000
	(Application money received)				
July 1	Share Application A/c	Dr.		50,000	
	To Share Capital A/c				50,000
	(Application money transferred to Share Capital Account)				

July 1	Share Allotment A/c	Dr.		50,000	
	To Share Capital A/c				50,000
	(Allotment money due)				
July 1	Bank A/c	Dr.		51,000	
	To Share Allotment A/c				50,000
	To Calls-in-Advance A/c (200 shares @ ₹5)				1,000
	(Allotment money received alongwith Calls-in-Advance)				
Oct. 1	Share First Call A/c	Dr.		40,000	
	To Share Capital A/c				40,000
	(First call money due)				
Oct. 1	Bank A/c	Dr.		39,600	
	Calls-in-Advance A/c (200 shares @ ₹2)	Dr.		400	
	To Share First Call A/c				40,000
	(First call money received and Calls-in-Advance adjusted)				
2022					
Feb. 1	Share Second and Final Call A/c	Dr.		60,000	
	To Share Capital A/c				60,000
	(Second and final call money due)				
Feb. 1	Bank A/c	Dr.		59,100	
	Calls-in-Advance A/c (200 shares @ ₹3)	Dr.		600	
	Calls-in-Arrears A/c (100 shares @ ₹3)	Dr.		300	
	To Share Second and Final Call A/c				60,000
	(Second and final call money received and Calls-in-Advance adjusted. Arrear on 100 shares @ ₹3 debited to Calls in Arrears Account)				
Feb. 1	Interest on Calls-in-Advance A/c	Dr.		18	
	To Sundry Members A/c				18
	(Interest due on Calls-in-Advance)				
Feb. 1	Sundry Members A/c	Dr.		18	
	To Bank A/c				18
	(Interest paid on Calls-in-Advance)				
March 31	Statement of Profit & Loss	Dr.		18	
	To Interest on Calls-in-Advance A/c				18
	(Interest on Calls in advance transferred to Statement of Profit & Loss)				

Working Note :

Calculation of Interest on Calls in Advance :			₹
On First Call money : (From 1st July to 1st Oct.)	$= 400 \times \frac{3}{12} \times \frac{4}{100}$	=	4
On Second Call money : (From 1st July to 1st Feb.)	$= 600 \times \frac{7}{12} \times \frac{4}{100}$	=	14
		Total	18

ILLUSTRATION 14.

A company issued 50,000 equity shares of ₹10 each at par payable as under :

On application ₹2; on allotment ₹1; on first call ₹3 and on final call ₹4 per share (four months after first call).

Amount due on application and allotment was duly received. One shareholder holding 1,000 shares could not pay the first call money in time. Another shareholder holding 2,000 shares paid the final call money alongwith the first call money.

Final call was made. All the shareholders paid in full. First call arrear on 1,000 shares alongwith interest on calls in arrears were also received at the time of final call. The company paid interest on calls in advance and charged interest on calls in arrears according to the provisions of Table F of schedule I of Companies Act, 2013.

Make entries in the company's journal for transactions relating to first call and final call.

SOLUTION :

JOURNAL

Date	*Particulars*		*L.F.*	*Dr.* (₹)	*Cr.* (₹)
	Equity Share First Call A/c	Dr.		1,50,000	
	To Equity Share Capital A/c				1,50,000
	(First call due on 50,000 shares @ ₹3 per share)				
	Bank A/c	Dr.		1,55,000	
	Calls-in-Arrears A/c (1,000 × ₹3)	Dr.		3,000	
	To Equity Share First Call A/c				1,50,000
	To Calls in Advance A/c (2,000 × ₹4)				8,000
	(First call money received except on 1,000 shares and final call received in advance on 2,000 shares)				
	Equity Share Final Call A/c	Dr.		2,00,000	
	To Equity Share Capital A/c				2,00,000
	(Final call due on 50,000 shares @ ₹4 per share)				
	Bank A/c	Dr.		1,92,000	
	Calls in Advance A/c	Dr.		8,000	
	To Equity Share Final Call A/c				2,00,000
	(Final Call money received after adjusting calls in advance)				
	Bank A/c	Dr.		3,000	
	To Calls-in-Arrears A/c				3,000
	(Calls in arrears received)				
	Interest on Calls in Advance A/c	Dr.		320	
	To Sundry Members A/c				320
	(Interest due on calls in advance : ₹8,000 × $\frac{12}{100} \times \frac{4}{12}$)				
	Sundry Members A/c	Dr.		320	
	To Bank A/c				320
	(Interest paid on calls in advance)				

	Sundry Members A/c Dr. To Interest on Calls in Arrears A/c (Interest due on calls in arrears : ₹3,000 × $\frac{10}{100} \times \frac{4}{12}$)		100	100
	Bank A/c Dr. To Sundry Members A/c (Interest received on calls in arrears)		100	100
	Statement of Profit & Loss Dr. To Interest on Calls in Advance A/c (Interest on Calls in Advance transferred to Statement of P & L)		320	320
	Interest on Calls in Arrears A/c Dr. To Statement of Profit & Loss (Interest on Calls in Arrears transferred to Statement of P & L)		100	100

ILLUSTRATION 15.

The Decoy Trading Company Limited was registered with a nominal capital of ₹1,00,000 in shares of ₹10 each, 9,000 of which were issued payable as : ₹2.50 on application, ₹2.50 on allotment, ₹3 on first call and the balance on final call. All the shares were applied for and allotted and all cash was received on the due dates except that one shareholder holding 100 shares failed to pay the allotment money and another shareholder holding 200 shares paid the first and final call together with allotment money.

You are required to journalise the above transactions in the books of the company particularly through calls in arrear account and calls in advance account as and when necessary.

SOLUTION : **Journal of Decoy Trading Company Ltd.**

Date	*Particulars*	*L.F.*	*Dr.*	*Cr.*
			₹	₹
	Bank A/c Dr. To Share Application A/c (Application money received on 9,000 shares @ ₹2.50 per share)		22,500	22,500
	Share Application A/c Dr. To Share Capital A/c (Transfer of application money to Share Capital A/c)		22,500	22,500
	Share Allotment A/c Dr. To Share Capital A/c (Allotment money due on 9,000 shares @ ₹2.50 per share)		22,500	22,500

	Bank A/c[1] Dr.		23,250	
	Calls in Arrears A/c (100 × ₹2.50) Dr.		250	
	To Share Allotment A/c			22,500
	To Calls in Advance A/c (200 × ₹5)			1,000
	(Allotment money received on 8,900 shares @ ₹2.50 per share and calls in advance received on 200 shares @ ₹7 per share; arrears of allotment money on 100 shares being debited to Calls-in-arrear A/c)			

Notes : **(1)** Amount received :

		₹
	On 8,900 shares @ ₹2.50 per share	22,250
+	On 200 shares @ ₹5 per share	1,000
		23,250

(2) Since the question is silent about receipt of first call or final call money, it is assumed that these two calls have not been made so far.

ILLUSTRATION 16.

Globe Ltd., with an authorised capital of 50,000 equity shares of ₹100 each of which 30,000 have already been issued, issues a prospectus offering the remaining 20,000 shares at a premium of ₹60 per share payable as follows :

₹50 on Application (including premium ₹30);
₹60 on Allotment (including premium ₹30);
₹25 on First Call;
Balance on Second and Final Call.

The issue was over-subscribed and ₹1,00,000 were repaid to unsuccessful applicants.

The amount due on allotment was received in full but the allotees of 500 shares defaulted on the first call and of 800 on the second call.

The issue costs amounted to ₹50,000.

You are required to :

(*a*) Record the above mentioned transactions of Globe Ltd. by way of Ledger Accounts.

(*b*) Show how the relevant items would appear in the Balance Sheet.

SOLUTION :

Globe Ltd.

Dr. BANK ACCOUNT Cr.

Particulars	₹	*Particulars*	₹
To Share Application A/c	11,00,000	By Share Application A/c	1,00,000
To Share Allotment A/c	12,00,000	By Share Issue Expenses A/c	50,000
To Share First Call A/c (19,500 × 25)	4,87,500	By Balance c/d	31,17,500
To Share Second & Final Call A/c (19,200 × ₹25)	4,80,000		
	32,67,500		32,67,500
To Balance b/d	31,17,500		

Dr. SHARE ISSUE EXPENSES ACCOUNT Cr.

Particulars	₹	Particulars	₹
To Bank A/c	50,000	By Securities Premium Reserve A/c (expenses written off)	50,000
	50,000		50,000

Dr. SHARE APPLICATION ACCOUNT Cr.

Particulars	₹	Particulars	₹
To Share Capital A/c	4,00,000	By Bank A/c	11,00,000
To Securities Premium Reserve A/c	6,00,000		
To Bank A/c	1,00,000		
	11,00,000		11,00,000

Dr. SHARE ALLOTMENT ACCOUNT Cr.

Particulars	₹	Particulars	₹
To Share Capital A/c	6,00,000	By Bank A/c	12,00,000
To Securities Premium Reserve A/c	6,00,000		
	12,00,000		12,00,000

Dr. SHARE FIRST CALL ACCOUNT Cr.

Particulars	₹	Particulars	₹
To Share Capital A/c	5,00,000	By Bank A/c	4,87,500
		By Calls in Arrear A/c	12,500
	5,00,000		5,00,000

Dr. SHARE SECOND & FINAL CALL ACCOUNT Cr.

Particulars	₹	Particulars	₹
To Share Capital A/c	5,00,000	By Bank A/c	4,80,000
		By Calls in Arrear A/c	20,000
	5,00,000		5,00,000

Dr. SHARE CAPITAL ACCOUNT Cr.

Particulars	₹	Particulars	₹
To Balance c/d	50,00,000	By Balance b/d	30,00,000
		By Share Application A/c	4,00,000
		By Share Allotment A/c	6,00,000
		By Share First Call A/c	5,00,000
		By Share Second & Final Call A/c	5,00,000
	50,00,000		50,00,000
		By Balance b/d	50,00,000

Dr. **SECURITIES PREMIUM RESERVE ACCOUNT** Cr.

Particulars	₹	Particulars	₹
To Share Issue Expenses A/c	50,000	By Share Application A/c	6,00,000
To Balance c/d	11,50,000	By Share Allotment A/c	6,00,000
	12,00,000		12,00,000
		By Balance b/d	11,50,000

Dr. **CALLS IN ARREAR ACCOUNT** Cr.

Particulars	₹	Particulars	₹
To Share First Call A/c	12,500	By Balance c/d	32,500
To Share Second & Final Call A/c	20,000		
	32,500		32,500
To Balance b/d	32,500		

Extract of Balance Sheet
of Globe Ltd.
as at ....

Particulars	Note No.	Amount Current year	Amount Previous year
		₹	₹
I. EQUITY AND LIABILITIES :			
Shareholder's Funds :			
(*a*) Share Capital	1	49,67,500	30,00,000
(*b*) Reserves and Surplus	2	11,50,000	—
II. ASSETS			
Current Assets :			
Cash and Bank Balance		31,17,500	

Notes to Accounts :

			₹
1. **Share Capital :**			
Authorised			
50,000 equity shares of ₹100 each			50,00,000
Issued			
50,000 equity shares of ₹100 each			50,00,000
Subscribed			
Subscribed and fully paid			
49,200 equity shares of ₹100 each		49,20,000	
Subscribed but not fully paid			
800 equity shares of ₹100 each fully called	80,000		
Less : Calls in arrear	32,500	47,500	49,67,500
2. **Reserves and Surplus :**			
Securities Premium Reserve			11,50,000

Over-Subscription of Shares

Shares issued by well managed and financially strong Companies often get over-subscribed. Shares are said to be over-subscribed when the number of shares applied for is more than the number of shares offered to the public for subscription. However, as the Company cannot allot shares more than that offered for subscription; the board of Directors will have to allot shares on **Pro-rata basis.** It means that smaller number of shares are allotted to each applicant according to the number of shares applied by him.

There may be some applicants who are not allotted any shares. The application money received from these applicants is returned to them. Following entry is passed for this purpose :

Share Application A/c Dr.
To Bank A/c
(Application money returned)

When some applicants are allotted smaller number of shares, the excess amount received on applications is utilised towards the amount due on allotment. Following entry is passed :

Share Application A/c Dr.
To Share Allotment A/c
(Excess Application money utilized for Allotment)

Sometimes the excess application money exceeds even the money due on allotment. Such amount has to be returned. However, it can be retained by the Company for its utilization towards future calls if the Articles so authorise. Usually the prospectus contains a clause to this effect. If the amount is retained, it must be transferred to calls in Advance A/c by passing the following entry :

Share Application A/c Dr.
To Share Allotment A/c
To Calls in Advance A/c
(Excess Application money utilized for Allotment and Calls)

Treatment of Surplus Application Money in Case of Pro-rata Allotment

(*i*) If the question is silent about the treatment of surplus application money or states that surplus application money will be adjusted only on allotment, then surplus application money will be used only for allotment and the balance, if still left, will be refunded.

(*ii*) If the question specifically states that surplus application money will be adjusted towards allotment and calls, then the surplus application money is transferred to allotment and calls in advance account. The balance, if still left, will be refunded.

ILLUSTRATION 17.

X Ltd. issued 30,000 shares of ₹10 each, payable as under :

₹3.00 on Application,	payable on 1st April, 2021
₹2.00 on Allotment,	payable on 1st June, 2021
₹2.50 on First Call,	payable on 1st Sept., 2021
₹2.50 on Final Call,	payable on 1st Feb., 2022

Applications were received for 50,000 shares and the allotments were made as under :

To applicants for 24,000 shares	.... Full
To applicants for 18,000 shares	 6,000
To applicants for 8,000 shares	.... Nil

Excess money received on application was utilised towards allotment and subsequent calls. Interest on calls in advance was paid @ 12% per annum.

On 15th February 2022, the company also allotted 800 shares of ₹10 each at the rate of ₹9 per share as sweat equity shares to the employees of the company.

Journalise the transactions, assuming all sums due were received and company closes its books every year on 31st March.

SOLUTION :

JOURNAL

Date	Particulars		L.F.	Dr	Cr.
2021				₹	₹
April 1	Bank A/c	Dr.		1,50,000	
	To Share Application A/c				1,50,000
	(Application money received on 50,000 shares)				
June 1	Share Application A/c	Dr.		1,50,000	
	To Share Capital A/c				90,000
	To Share Allotment A/c				12,000
	To Calls in Advance A/c				24,000(1)
	To Bank A/c				24,000
	(Transfer of application money on 30,000 shares @ ₹3 to Share Capital a/c; on 6,000 shares @ ₹2 to Share Allotment a/c and the excess amount to Calls in Advance A/c and amount returned on 8,000 shares)				
June 1	Share Allotment A/c	Dr.		60,000	
	To Share Capital A/c				60,000
	(Allotment due on 30,000 shares)				
June 1	Bank A/c	Dr.		48,000	
	To Share Allotment A/c				48,000
	(Allotment money received less ₹12,000 received alongwith applications)				
Sept. 1	Share First Call A/c	Dr.		75,000	
	To Share Capital A/c				75,000
	(First call due on 30,000 shares)				
Sept. 1	Bank A/c	Dr.		60,000	
	Calls in Advance A/c	Dr.		15,000	
	To Share First Call A/c				75,000
	(First call money received less ₹15,000 received in advance)				

2022 Feb. 1	Share Final Call A/c Dr. To Share Capital A/c (Final Call due on 30,000 shares)		75,000	75,000
Feb. 1	Bank A/c Dr. Calls in Advance A/c Dr. To Share Final Call A/c (Amount received on final call after adjustment of calls in advance money)		66,000 9,000	75,000
Feb. 1	Interest on Calls in Advance A/c Dr. To Bank A/c (Interest on calls in advance)		1,170(2)	1,170
Feb. 15	Bank A/c Dr. Share Discount A/c Dr. To Share Capital A/c (Allotment of 800 sweat equity shares @ ₹9 each to the employees of the company)		7,200 800	8,000
March 31	Statement of Profit and Loss Dr. To Interest on Calls in Advance A/c (Interest on calls in advance transferred to Statement of P & L)		1,170	1,170

Working Notes :

(1) Applicants for 18,000 shares have been allotted 6,000 shares. Hence, excess application money received

On 12,000 shares @ ₹3 per share = ₹36,000

Less : Amount adjusted on Allotment on 6,000 shares @ ₹2 per share = ₹12,000

Balance = ₹24,000

This amount of ₹24,000 will be transferred to Calls in Advance A/c, as it will be adjusted on future calls.

Less : Amount adjusted on Ist Call on 6,000 shares @ ₹2.50 per share = ₹15,000

Balance = ₹ 9,000

This amount of ₹9,000 will be adjusted on Second Call.

(2) Interest will be allowed only on ₹24,000, as interest is allowed only on that amount which is transferred to 'Calls in Advance A/c'.

Out of this amount :

Interest on ₹15,000 will be allowed from Allotment to First Call, *i.e.*, for 3 months.

Interest on ₹ 9,000 will be allowed from Allotment to Second Call, *i.e.*, for 8 months.

$$15{,}000 \times \frac{12}{100} \times \frac{3}{12} = ₹\ 450$$

$$9{,}000 \times \frac{12}{100} \times \frac{8}{12} = ₹\ 720$$

Total Interest = ₹1,170

Opening of Joint 'Application and Allotment Account' : Now-a-days it is becoming a common practice to open only one account for application and allotment instead of two separate accounts. In such a case a joint account named "Application and Allotment Account" is opened and all entries relating to application and allotment are made in this account.

When a joint account is maintained, the journal entries are recorded in the following manner :

(*i*) On receipt of Application money :

Bank A/c Dr. [No. of shares applied × Application money per share]
To Share Application and Allotment A/c

(*ii*) On transfer of Application money and Allotment amount due :

Share Application and Allotment A/c Dr. [No. of shares Allotted × (Application money per share + Allotment amount per share)]
To Share Capital A/c

(*iii*) On refund of money on rejected applications :

Share Application and Allotment A/c Dr. [No. of shares Rejected × Application money per share]
To Bank A/c

(*iv*) On receipt of balance of Allotment money :

Bank A/c Dr.
To Share Application and Allotment A/c

ILLUSTRATION 18.

On April 1, 2022, a Limited Company was incorporated with an authorised capital of ₹8,00,000 divided into shares of ₹10 each.

It offered to the public for subscription of 60,000 shares payable as follows :

On Application	₹3 per share
On Allotment (May 1, 2022)	₹2 per share
On First and Final Call (One month after allotment)	₹5 per share

Public applied for 92,000 shares and the application money was duly received on April 15, 2022. Applications for 2,000 shares were rejected and applicants for 90,000 shares were allotted 60,000 shares.

Give journal entries to record the transactions in the books of the company if :

(*i*) The amount due has been duly received.

(*ii*) The company maintains the combined account for application and allotment.

SOLUTION:

JOURNAL

Date	*Particulars*	*L.F.*	*Dr.*	*Cr.*
2022			₹	₹
April 15	Bank A/c Dr.		2,76,000	
	To Share Application and Allotment A/c			2,76,000
	(Application money received on 92,000 shares @ ₹3 per share)			

May 1	Share Application and Allotment A/c To Share Capital A/c (Transfer of application money @ ₹3 and allotment money due @ ₹2 on 60,000 shares)	Dr.		3,00,000	3,00,000(1)
May 1	Share Application and Allotment A/c To Bank A/c (Application money refunded on rejected applications : 2,000 shares @ ₹3)	Dr.		6,000	6,000
May 1	Bank A/c To Share Application and Allotment A/c (Balance of allotment money received)	Dr.		30,000(3)	30,000
June 1	Share First and Final Call A/c To Share Capital A/c (First and Final Call due on 60,000 shares)	Dr.		3,00,000	3,00,000
June 1	Bank A/c To Share First and Final Call A/c (First and final call money received)	Dr.		3,00,000	3,00,000

(1) Only one entry is passed for crediting the Share Capital Account in respect of both the application money and the allotment money.

(2) Entry for surplus application money to be adjusted on allotment need not be passed.

		₹
(3) Amount due on allotment : 60,000 shares × ₹2	=	1,20,000
Less : Excess received on application : 30,000 shares × ₹3	=	90,000
		30,000

(4) There will be no change in the entries in respect of Calls on Shares.

Forfeiture of Shares

If any shareholder fails to pay the amount due on allotment or on any call within the specified period, the Directors may cancel his shares. This is called Forfeiture of Shares.

It may be noted that the shares can be forfeited only if the Articles of Association of the Company allow them to be forfeited. In order to make the forfeiture valid, it is essential to follow the rules laid down in the Articles. If no rules are given in Articles, the provisions of Table F of Schedule I of the Companies Act, 2013 regarding forfeiture apply. The usual procedure is that the defaulting shareholder must be given a minimum of 14 days' notice requiring him to pay the unpaid amount on his shares together with the accrued interest thereon. The notice must state that if the unpaid amount is not paid within a certain period, his shares shall be forfeited. If, in spite of this notice, the shareholder still does not pay the unpaid amount on his shares, his shares may be forfeited by a resolution of the Board of Directors.

After the forfeiture, the name of the shareholder is removed from the Register of Members. The amount already paid by him belongs to the Company and is not returned to him.

Entries on Forfeiture of Shares

(1) **Forfeiture of Shares which were issued at Par :** On forfeiture of shares the Share Capital is reduced and as such, 'Share Capital A/c' is debited for the amount which has been called so far on the forfeited shares; Calls in Arrear A/c is credited in order to cancel the debit balance of Calls in Arrears A/c standing in the books. The amount already paid by the defaulting shareholder is Credited to 'Share Forfeiture A/c'.

The Journal Entry is :

Share Capital A/c	Dr.	(Number of Shares forfeited × Called up Value per share)
To Calls in Arrears A/c		(Amount not received on Allotment & Calls)
To Share Forfeiture A/c		(Amount received on Application, Allotment and Calls so far)
(Forfeiture of Shares issued at Par)		

Example 1 : Gopal was holding 100 shares of ₹10 each of a Company on which he had paid ₹3 on application and ₹2 on allotment, but could not pay ₹2 on first call. If the shares of Gopal are forfeited by the Directors, the entry for the forfeiture of shares will be :

Share Capital A/c	Dr.	700	
To Calls in Arrears A/c			200
To Share Forfeiture A/c			500
(100 shares forfeited for non-payment of first call of ₹2)			

(2) **Forfeiture of Shares which were issued at Premium :** This may be discussed under two heads :

(I) **When forfeiture takes place after the premium is received :** According to Section 52 of Companies Act 2013, if premium has been fully collected, it cannot be cancelled even if that share is forfeited later on. As such, 'Securities Premium Reserve A/c' will not be debited in the entry for forfeiture in this case.

(II) **When forfeiture takes place before the premium is received :** When a share is forfeited on which the premium has become due but has not been received either wholly or partially, the 'Securities Premium Reserve A/c' must be debited with the amount of premium not received in the entry for forfeiture. The entry in this case will be :

Share Capital A/c	Dr.	(Amount called up so far, excluding premium)
Securities Premium Reserve A/c	Dr.	(If the premium has not been received)
To Calls in Arrears A/c		(Amount not received on Allotment and Calls including premium)
To Share Forfeiture A/c		(Amount received on Application, Allotment and Calls so far)
(Forfeiture of shares issued at Premium)		

Example 2 : *X* Ltd. issued 100 shares of ₹10 each to Gopal at a premium of ₹4 per share. Only ₹3.50 per share have been received on these shares on Application. Gopal has not paid ₹6.50 on Allotment (including premium), ₹2 on First Call and ₹2 on Final Call.

Entry for the forfeiture of above shares will be :

Share Capital A/c	Dr.	1,000	
Securities Premium Reserve A/c	Dr.	400	
To Calls in Arrears A/c			1,050
To Share Forfeiture A/c			350
(Forfeiture of 100 shares)			

Note : In the above case the amount of premium was due on allotment. Gopal could not pay the amount due on allotment and as such he could not pay the amount of premium also. Hence, the 'Securities Premium Reserve A/c' will be debited in the entry for forfeiture.

Example 3 : If, in the above Example No. 2, it is assumed that Gopal had paid the amount of Application and Allotment as well, and only calls are not received from him, the entry for the forfeiture of shares will be as under :

Share Capital A/c	Dr.	1,000	
To Calls in Arrears A/c			400
To Share Forfeiture A/c			600

Re-Issue of Forfeited Shares

Directors have the authority to reissue the forfeited shares on such terms as they think fit. That is to say that they are at liberty to reissue the forfeited shares at par, at premium or at discount. However, if the shares are re-issued at a discount the amount of the discount cannot exceed the amount previously received on these shares.

For example, if a share of ₹10, on which ₹3 has already been received, is forfeited and reissued, minimum ₹7 must be collected on its reissue. It means that maximum of ₹3 can be allowed as discount on the reissue of such shares.

Following entries are passed on the reissue of forfeited shares :

I. If the Forfeited Shares are reissued at par :

Bank A/c	Dr.
To Share Capital A/c	

II. If the Forfeited Shares are reissued at Premium :

Bank A/c	Dr.
To Share Capital A/c	
To Securities Premium Reserve A/c	

III. If the Forfeited Shares are reissued at Discount :

Bank A/c	Dr.
Share Forfeiture A/c	Dr.
To Share Capital A/c	

After the reissue of forfeited shares, the credit balance left in the Share Forfeiture A/c is a 'Capital Gain' to the Company and must be transferred to 'Capital Reserve A/c'. The journal entry for such Transfer will be :

Share Forfeiture A/c	Dr.
To Capital Reserve A/c	
(Transfer of Share Forfeiture A/c to Capital Reserve A/c)	

It should be clearly understood that if all the forfeited shares are not re-issued, only that proportion of share forfeiture account which belongs to the re-issued shares should only be transferred to Capital Reserve Account.

ILLUSTRATION 19.

Pawan Ltd. was registered with an authorised Capital of ₹5,00,000 divided into shares of ₹10 each. It purchased a Building from *Y* for ₹2,00,000 and issued fully paid shares to *Y* for purchase consideration. It invited applications for the balance 30,000 shares payable as under :—₹3 per share on Application; ₹3 per share on Allotment; ₹2 per share on First Call; and ₹2 on Final Call.

Ashok, who had been allotted 500 shares failed to pay both the Calls. His shares were forfeited and re-issued at ₹9 per share to Hari, as fully paid up. Make necessary entries in the Journal and also prepare the opening balance sheet of the company.

SOLUTION :

JOURNAL

Date	Particulars		L.F.	Dr.	Cr.
				₹	₹
	Buildings A/c	Dr.		2,00,000	
	To Vendors (*Y*)				2,00,000
	(Assets purchased)				
	Vendors (*Y*)	Dr.		2,00,000	
	To Share Capital A/c				2,00,000
	(Purchase consideration discharged by shares)				
	Bank A/c	Dr.		90,000	
	To Share Application A/c				90,000
	(Amount received on application)				
	Share Application A/c	Dr.		90,000	
	To Share Capital A/c				90,000
	(Amount of share application transferred to share capital A/c)				
	Share Allotment A/c	Dr.		90,000	
	To Share Capital A/c				90,000
	(Allotment due)				
	Bank A/c	Dr.		90,000	
	To Share Allotment A/c				90,000
	(Amount received on allotment)				
	Share First Call A/c	Dr.		60,000	
	To Share Capital A/c				60,000
	(Amount due on first call)				
	Bank A/c	Dr.		59,000	
	Calls in Arrears A/c*	Dr.		1,000	
	To Share First Call A/c				60,000
	(Amount received on first call on 29,500 shares @ ₹2 per share)				

	Share Final Call A/c Dr.		60,000	
	To Share Capital A/c			60,000
	(Amount due on Final call)			
	Bank A/c Dr.		59,000	
	Calls in Arrears A/c* Dr.		1,000	
	To Share Final Call A/c			60,000
	(Amount received on final call on 29,500 shares @ ₹2 per share)			
	Share Capital A/c Dr.		5,000	
	To Calls in Arrears A/c			2,000
	To Share Forfeiture A/c			3,000
	(500 shares of Ashok forfeited for non-payment of First Call and Final Call)			
	Bank A/c Dr.		4,500	
	Share Forfeiture A/c Dr.		500	
	To Share Capital A/c			5,000
	(Re-issue of 500 shares @ ₹9 per share)			
	Share Forfeiture A/c Dr.		2,500	
	To Capital Reserve A/c			2,500
	(Balance left in Share Forfeiture A/c ₹3,000 – ₹500 = ₹2,500 transferred to Capital Reserve A/c)			

*As per revised ISC Syllabus, when allotment or any Call money is not received, it is to be debited to Calls in Arrears A/c.

BALANCE SHEET OF PAWAN LTD.

as at ....

Particulars	*Note No.*	*Current year*	*Previous year*
I. EQUITY AND LIABILITIES :		₹	₹
Shareholder's Funds :			
(*a*) Share Capital	1	5,00,000	
(*b*) Reserve and Surplus	2	2,500	
		5,02,500	
II. ASSETS :			
Non-Current Assets :			
Fixed Assets :			
(*i*) Tangible Assets	3	2,00,000	
Current Assets :			
Cash and Bank Balance	4	3,02,500	
		5,02,500	

Notes to Accounts :

	₹	₹
(1) **Share Capital**		
Authorised, Issued, Subscribed and fully paid Capital :		
20,000 Shares of ₹10 each allotted as fully paid for a consideration other than cash	2,00,000	
30,000 Shares of ₹10 each fully paid up	3,00,000	
	5,00,000	
(2) **Reserve and Surplus :**		
Capital Reserve	2,500	
(3) **Tangible Assets :**		
Building	2,00,000	
(4) **Cash and Bank Balance :**		
Cash at Bank	3,02,500	

ILLUSTRATION 20.

X Limited invited applications for 20,000 shares of ₹10 each payable as under : ₹3 per share on application; ₹3 per share on Allotment; ₹2 per share on First Call; and ₹2 per share on Final Call.

Final Call was not made by the company. An applicant who had been allotted 100 shares failed to pay Allotment and First Call money due from him. His shares were forfeited after the First Call and were immediately re-issued at ₹8.50 per share. Make necessary entries in the Journal and prepare the opening balance sheet of the company.

SOLUTION : JOURNAL OF *X* LTD.

Date	*Particulars*		*L.F*	*Dr*	*Cr.*
				₹	₹
	Bank A/c	Dr.		60,000	
	To Share Application A/c				60,000
	(Amount received on applications)				
	Share Application A/c	Dr.		60,000	
	To Share Capital A/c				60,000
	(Amount of Share application transferred to Share Capital A/c)				
	Share Allotment A/c	Dr.		60,000	
	To Share Capital A/c				60,000
	(Allotment due)				
	Bank A/c	Dr.		59,700	
	Calls in Arrears A/c	Dr.		300	
	To Share Allotment A/c				60,000
	(Amount received on allotment on 19,900 shares @ ₹3 per share)				
	Share First Call A/c	Dr.		40,000	
	To Share Capital A/c				40,000
	(First call due)				

	Bank A/c Dr. Calls in Arrears A/c Dr. To Share First Call A/c (First call received on 19,900 shares @ ₹2 per share)		39,800 200	 40,000
	Share Capital A/c Dr. To Calls in Arrears A/c To Share Forfeiture A/c (100 shares forfeited for non-payment of allotment & first call)		800(1)	 500 300
	Bank A/c Dr. To Share Capital A/c To Securities Premium Reserve A/c (Re-issue of 100 forfeited shares @ ₹8.50 per share)		850	 800 50
	Share Forfeiture A/c Dr. To Capital Reserve A/c (Transfer of Share Forfeiture A/c to Capital Reserve A/c)		300	 300

BALANCE SHEET OF *X* LTD.

as at ....

Particulars	*Note No.*	*Current year*	*Previous year*
I. EQUITY AND LIABILITIES :		₹	₹
Shareholder's Funds :			
(*a*) Share Capital	1	1,60,000	
(*b*) Reserve and Surplus	2	350	
		1,60,350	
II. ASSETS :			
Current Assets :			
Cash and Bank Balance	3	1,60,350	

Notes to Accounts :

	₹	₹
(1) **Share Capital :**		
Authorised Capital :		
.... Shares of ₹........ each	....	
Issued and Subscribed Share Capital :		
20,000 Shares of ₹10 each	2,00,000	
Subscribed but not fully paid Capital :		
20,000 Shares of ₹10 each, ₹8 per share paid up	1,60,000	
(2) **Reserves and Surplus :**		
Capital Reserve	300	
Securities Premium Reserve A/c	50	
	350	

(3) Cash and Bank Balance : Cash at Bank	1,60,350	

Hint : (1) Final Call of ₹2 per share has not been made in the question, as such only ₹8 have been called up. Therefore, Share Capital A/c will be debited only from ₹8 per share at the time of forfeiture of shares.

ILLUSTRATION 21.

Dinesh Ltd. invited applications for issuing 10,000 Equity shares of ₹10 each. The amount was payable as follows :

On Application	₹1
On Allotment	₹2
On First Call	₹3
On Second and Final Call	Balance

The issue was fully subscribed. Ram to whom 100 shares were allotted, failed to pay the allotment money and his shares were forfeited immediately after allotment. Shyam to whom 150 shares were allotted, failed to pay the first call. His shares were also forfeited after the first call. Afterwards the second and final call was made. Mohan to whom 50 shares were allotted failed to pay the second and final call. His shares were also forfeited. All the forfeited shares were re-issued at ₹9 per share fully paid up. Pass necessary journal entries in the books of Dinesh Ltd.

SOLUTION : JOURNAL OF DINESH LTD.

Date	*Particulars*		*L.F.*	*Dr.*	*Cr.*
				₹	₹
	Bank A/c To Equity Share Application A/c (Application money received)	Dr.		10,000	 10,000
	Equity Share Application A/c To Equity Share Capital A/c (Application money transferred to Share Capital A/c)	Dr.		10,000	 10,000
	Equity Share Allotment A/c To Equity Share Capital A/c (Allotment money due on 10,000 shares)	Dr.		20,0[illegible]	 20,000
	Bank A/c Calls in Arrears A/c To Equity Share Allotment A/c (Allotment money received except on 100 shares)	Dr. Dr.		19,800 200	 20,000
	Equity Share Capital A/c (100 × ₹3) To Calls in Arrears A/c (100 × ₹2) To Forfeited Shares A/c (100 × ₹1) (100 shares forfeited for non-payment of allotment money)	Dr.		300	 200 100
	Equity Share First Call A/c To Equity Share Capital A/c (First call money due on 9,900 shares @ ₹3 per share)	Dr.		29,700	 29,700

	Bank A/c Dr.		29,250	
	Calls in Arrears A/c Dr.		450	
	To Equity Share First Call A/c			29,700
	(First call money received except on 150 shares)			
	Equity Share Capital A/c (150 × ₹6) Dr.		900	
	To Calls in Arrears A/c (150 × ₹3)			450
	To Forfeited Shares A/c (150 × ₹3)			450
	(150 shares forfeited due to non-payment of first call money)			
	Equity Share Second & Final Call A/c Dr.		39,000	
	To Equity Share Capital A/c			39,000
	(Second & Final Call money due on 9,750 shares @ ₹4 per share)			
	Bank A/c Dr.		38,800	
	Calls in Arrears A/c Dr.		200	
	To Equity Share Second & Final Call A/c			39,000
	(Final call money received except on 50 shares)			
	Equity Share Capital A/c (50 × ₹10) Dr.		500	
	To Calls in Arrears A/c (50 × ₹4)			200
	To Forfeited Shares A/c (50 × ₹6)			300
	(50 shares forfeited due to non-payment of second call)			
	Bank A/c (300 × ₹9) Dr.		2,700	
	Forfeited Shares A/c (300 × ₹1) Dr.		300	
	To Equity Share Capital A/c			3,000
	(All 300 shares re-issued at ₹9 per share fully paid up)			
	Forfeited Shares A/c[1] Dr.		550	
	To Capital Reserve A/c			550
	(Gain on re-issue transferred to Capital Reserve A/c)			

Note : (1)

	₹
Forfeited amount on 100 Shares of Ram	100
Forfeited amount on 150 Shares of Shyam	450
Forfeited amount on 50 Shares of Mohan	300
	850
Less : Loss on Re-issue	300
Transferred to Capital Reserve	550

ILLUSTRATION 22.

A Ltd. makes an issue of 10,000 equity shares of ₹100 each, payable as follows:

On application and allotment	₹50
On first call	₹25
On second and final call	₹25

Members holding 400 shares did not pay the second call and the shares are duly forfeited, 300 of which are re-issued as fully paid at ₹80 per share. Pass Journal entries and prepare Share Capital and Forfeited Shares Account in the books of the company.

Also prepare the Balance Sheet.

SOLUTION : JOURNAL OF *A* LTD.

Date	*Particulars*	*L.F.*	*Dr.*	*Cr.*
			₹	₹
	Bank A/c Dr. To Equity Share Application and Allotment A/c (Application and allotment money received)		5,00,000	5,00,000
	Equity Share Application and Allotment A/c Dr. To Equity Share capital A/c (Aapplication and allotment money transferred)		5,00,000	5,00,000
	Equity Share First Call A/c Dr. To Equity Share capital A/c (First call money due)		2,50,000	2,50,000
	Bank A/c Dr. To Equity Share First Call A/c (First call money received)		2,50,000	2,50,000
	Equity Share Second & Final Call A/c Dr. To Equity Share Capital A/c (Second call money due)		2,50,000	2,50,000
	Bank A/c Dr. Calls in Arrears A/c Dr. To Equity Share Second & Final Call A/c (Share second call money received)		2,40,000 10,000	 2,50,000
	Equity Share Capital A/c Dr. To Calls in Arrears A/c To Forfeited Shares A/c (Forfeiture of 400 shares)		40,000	 10,000 30,000
	Bank A/c Dr. Forfeited Shares A/c Dr. To Equity Share Capital A/c (300 shares re-issued at ₹80 per share)		24,000 6,000	 30,000
	Forfeited Shares A/c[(3)] Dr. To Capital Reserve A/c (Gain on 300 forfeited shares transferred to Capital Reserve A/c)		16,500	16,500

Dr. EQUITY SHARE CAPITAL ACCOUNT Cr.

Particulars	₹	*Particulars*	₹
To Calls in Arrears A/c	10,000	By Equity Share Application & Allotment A/c	5,00,000
To Forfeited Shares A/c	30,000	By Equity Share First Call A/c	2,50,000
To Balance c/d	9,90,000	By Equity Share Second & Final Call A/c	2,50,000

		By Bank A/c	24,000
		By Forfeited Shares A/c	6,000
	10,30,000		10,30,000

Dr. FORFEITED SHARES ACCOUNT Cr.

Particulars	₹	*Particulars*	₹
To Equity Share Capital A/c	6,000	By Equity Share Capital A/c	30,000
To Capital Reserve A/c	16,500		
To Balance c/d	7,500		
	30,000		30,000

BALANCE SHEET OF *A* LTD.

as at..............

Particulars	*Note No.*	*Current year*	*Previous year*
I. EQUITY AND LIABILITIES :		₹	₹
Shareholder's Funds :			
(*a*) Share Capital	1	9,97,500	
(*b*) Reserve and Surplus Capital Reserve		16,500	
		10,14,000	
II. ASSETS :			
Current Assets :			
Cash and Bank Balance	2	10,14,000	

Notes to Accounts :

		₹	₹
(1) **Share Capital :**			
Authorised Capital :			
.... Shares of ₹........ each		....	
Issued Share Capital :			
10,000 Equity Shares of ₹100 each		10,00,000	
Subscribed and fully paid Capital:			
9,900 Equity Shares of ₹100 each fully paid	9,90,000		
Add : Forfeited Shares A/c	7,500(4)	9,97,500	
(2) **Cash and Bank Balance :**			
Cash at Bank		10,14,000	

Note (3) : Only that amount of gain is transferred from Forfeited Shares A/c to Capital Reserve A/c which belongs to the re-issued shares. In this question only 300 shares have been re-issued, as such, gain on only 300 shares will be transferred to Capital Reserve Account. This has been calculated as under :

As forfeited amount on 400 Shares = ₹30,000

Therefore, forfeited amount on 300 Shares $= \frac{30,000}{400} \times 300$ = ₹22,500

Less : Loss on the reissue of 300 shares (300 shares × ₹20) = 6,000

Transfer to Capital Reserve = 16,500

Note (4) : Balance left in forfeited shares account will be related to those shares which have not been reissued by the Company.

		₹
As forfeited amount on 400 shares	=	30,000
Therefore, forfeited amount on 100 Shares	=	$\frac{30,000}{400} \times 100$ = ₹7,500

ILLUSTRATION 23.

Pluto Ltd. issued 20,000 Equity Shares of ₹10 each, payable as follows :

On Application	₹4
On Allotment	₹1
On 1st Call	₹3
On 2nd and Final Call	₹2

Applications were received for 30,000 shares and pro-rata allotment was made to all the applicants.

Excess money received on application was utilised towards allotment and subsequent calls. One shareholder holding 100 shares did not pay the final call and his shares were forfeited. Of the forfeited shares, the company reissued 70 shares as fully paid up at ₹12 per share.

You are required to pass journal entries in the books of the company for the year ending 31st March, 2014. *(ISC, 2015)*

Journal of Pluto Ltd.

Date	*Particulars*		*L.F.*	*Dr.*	*Cr.*
				₹	₹
	Bank A/c	Dr.		1,20,000	
	To Share Application A/c				1,20,000
	(Share application money received)				
	Share Application A/c	Dr.		1,20,000	
	To Share Capital A/c				80,000
	To Share Allotment A/c				20,000
	To Calls in Advance A/c				20,000
	(Share application money transferred to share capital, surplus to share allotment and Calls-in-advance)				
	Shar Allotment A/c	Dr.		20,000	
	To Share Capital A/c				20,000
	(Share allotment due)				
	Share 1st Call A/c	Dr.		60,000	
	To Share Capital A/c				60,000
	(Share 1st Call due)				

	Bank A/c Dr.		40,000	
	Calls-in-Advance A/c Dr.		20,000	
	To Share 1st Call A/c			60,000
	(Share 1st Call received)			
	Share 2nd and Final Call A/c Dr.		40,000	
	To Share Capital A/c			40,000
	(Share 2nd and Final Call due)			
	Bank A/c Dr.		39,800	
	Calls in Arrears A/c Dr.		200	
	To Share 2nd and Final Call A/c			40,000
	(Share 2nd and Final Call received on 19,900 Shares)			
	Share Capital A/c Dr.		1,000	
	To Share Forfeiture A/c			800
	To Calls in Arrears A/c			200
	(100 Shares forfeited)			
	Bank A/c Dr.		840	
	To Share Capital A/c			700
	To Securities Premium Reserve A/c			140
	(70 Shares reissued @ ₹12 each)			
	Share Forfeiture A/c(2) Dr.		560	
	To Capital Reserve A/c			560
	(Net gain on forfeited shares transferred to Capital Reserve)			

Working Notes :

(1) Since all amount due on allotment has already been received on application there would be no entry for receipt of allotment money.

(2) Forfeited amount on 100 shares = ₹800

Hence, forfeited amount on 70 shares = $\frac{800}{100} \times 70$ = ₹560

ILLUSTRATION 24 (A).

A limited Company was registered with an authorised capital of ₹2,00,000 in ₹10 shares, of these 6,000 shares were issued as fully paid to the vendors for the purchase of buildings. 8,000 shares were subscribed for by the public and during the first year ₹6 per share were called up, payable ₹3 on application, ₹1 on allotment, ₹1 on first call, and ₹1 on second call. The amounts received in respect of these shares were as follows :

On 6,000 shares the full amount called.
On 1,200 shares ₹5 per share.
On 500 shares ₹4 per share.
On 300 shares ₹3 per share.

The directors forfeited 800 shares on which less than ₹5 per share had been paid.

Show journal entries in the books of the company and also show the Share Capital, as it would appear in the Balance Sheet.

SOLUTION : JOURNAL

Date	*Particulars*		*L.F.*	*Dr.* ₹	*Cr.* ₹
	Building A/c	Dr.		60,000	
	To Vendors A/c				60,000
	(Building purchased)				
	Vendors A/c	Dr.		60,000	
	To Share Capital A/c				60,000
	(Shares issued to vendors)				
	Bank A/c	Dr.		24,000	
	To Share Application A/c				24,000
	(Application money received on 8,000 shares @ ₹3 per share)				
	Share Application A/c	Dr.		24,000	
	To Share Capital A/c				24,000
	(Application money transferred to share capital account)				
	Share Allotment A/c	Dr.		8,000	
	To Share Capital A/c				8,000
	(Allotment due @ ₹1 per share on 8,000 shares)				
	Bank A/c	Dr.		7,700	
	Calls in Arrears A/c	Dr.		300	
	To Share Allotment A/c				8,000
	(Allotment money received on 7,700 shares)				
	Share First Call A/c	Dr.		8,000	
	To Share Capital A/c				8,000
	(First call due @ ₹1 per share on 8,000 shares)				
	Bank A/c	Dr.		7,200	
	Calls in Arrears A/c	Dr.		800	
	To Share First Call A/c				8,000
	(First call money received on 7,200 shares)				
	Share Second Call A/c	Dr.		8,000	
	To Share Capital A/c				8,000
	(Second call due on 8,000 shares @ ₹1 per share)				
	Bank A/c	Dr.		6,000	
	Calls in Arrears A/c	Dr.		2,000	
	To Share Second Call A/c				8,000
	(Second call money received on 6,000 shares)				
	Share Capital A/c (800 shares × ₹6)	Dr.		4,800	
	To Calls in Arrears A/c(3)				1,900
	To Share Forfeiture A/c				2,900
	(800 shares forfeited)				

EXTRACT OF BALANCE SHEET

as at ....

Particulars	*Note No.*	*Current year*	*Previous year*
I. EQUITY AND LIABILITIES :		₹	₹
Shareholder's Funds :			
(*a*) Share Capital	1	1,04,900	

Notes to Accounts :

		₹	₹
(1) **Share Capital :**			
Authorised Capital :			
20,000 Shares of ₹10 each		2,00,000	
Issued Capital :			
14,000 Shares of ₹10 each		1,40,000	
Subscribed Capital:			
Subscribed and Fully Paid up Capital:			
6,000 Shares of ₹10 each allotted as fully paid for consideration other than cash		60,000	
Subscribed but not Fully Paid Capital :			
7,200 Shares of ₹10 each, ₹6 called up	43,200		
Less : Calls in Arrears	1,200(2)		
	42,000		
Add : Share Forfeiture A/c	2,900	44,900	
		1,04,900	

Note : (2) ₹1 per share on 1,200 unforfeited shares.
(3) ₹2 per share on 500 shares and ₹3 per share on 300 shares.

ILLUSTRATION 24 (B).

In 2010, Ganga Ltd. was registered with an authorized capital of ₹1,00,000 in Equity shares of ₹10 each. Of these, 4,000 equity shares were issued as fully paid to vendors for the purchase of Plant and Machinery and the remaining 6,000 shares were subscribed for by the public for cash. During the first year, ₹6 per equity share was called up on these 6,000 shares, payable ₹3 on application, ₹1 on allotment and ₹2 on the first call.

The amount received in respect of these shares were as follows :

On 5,000 shares, the full amount called.

On 600 shares, ₹4 per share.

On 400 shares, ₹3 per share.

The company forfeited all those shares on which only ₹3 had been received and reissued them at ₹4 per share, ₹6 called up.

Journalise the transactions in the books of the company and prepare a Calls-in-Arrear Account. *(I.S.C. 2012)*

SOLUTION : JOURNAL OF GANGA LTD.

Date	Particulars	L.F.	Dr.	Cr.
			₹	₹
	Plant and Machinery A/c Dr.		40,000	
	To Vendors A/c			40,000
	(Purchase of Plant and Machinery)			
	Vendors A/c Dr.		40,000	
	To Equity Share Capital A/c			40,000
	(Shares issued to vendors)			
	Bank A/c Dr.		18,000	
	To Equity Share Application A/c			18,000
	(Application money received on 6,000shares @₹3 per share)			
	Equity Share Application A/c Dr.		18,000	
	To Equity Share Capital A/c			18,000
	(Application money transferred to share capital account)			
	Equity Share Allotment A/c Dr.		6,000	
	To Equity Share Capital A/c			6,000
	(Allotment due @₹1 per share on 6,000 shares)			
	Bank A/c Dr.		5,600	
	Calls in Arrear A/c Dr.		400	
	To Equity Share Allotment A/c			6,000
	(Allotment money received on 5,600 shares)			
	Equity Share First Call A/c Dr.		12,000	
	To Equity Share Capital A/c			12,000
	(First call due @₹2 per share on 6,000 shares)			
	Bank A/c Dr.		10,000	
	Calls in Arrear A/c Dr.		2,000	
	To Equity Share First Call A/c			12,000
	(First call money received on 5,000 shares)			
	Equity Share Capital A/c (400 shares × ₹6) Dr.		2,400	
	To Calls in Arrear A/c (400 Shares × ₹3)			1,200
	To Share Forfeiture A/c			1,200
	(400 shares forfeited)			
	Bank A/c Dr.		1,600	
	Share Forfeiture A/c Dr.		800	
	To Equity Share Capital A/c			2,400
	(Re-issue of 400 Shares @ ₹4 per share, ₹6 called-up)			
	Share Forfeiture A/c Dr.		400	
	To Capital Reserve A/c			400
	(Profit on forfeiture transferred to Capital Reserve)			

Dr. CALLS IN ARREAR ACCOUNT Cr.

Particulars	₹	Particulars	₹
To Equity Share Allotment A/c	400	By Equity Share Capital A/c	1,200
To Equity Share First Call A/c	2,000	By Balance c/d	1,200
	2,400		2,400

ILLUSTRATION 25.

'Scooters India Ltd.' is registered with an authorized capital of ₹50,00,000, divided into 5,00,000 shares of ₹10 each. The company issued 1,00,000 shares for subscriptions to the public at a premium of ₹2 per share. The amount was payable as follows :

On Application and Allotment — ₹3 per share
On 1st Call — ₹4 per share (including premium ₹2)
On 2nd and Final Call — ₹5 per share

Applications were received for 1,20,000 shares and allotment was made pro-rata to all applicants. All calls were made and were duly received except the 2nd and final call on 1,000 shares held by Rohan. His shares were forfeited and afterwards re-issued at ₹8 per share as fully paid up.

Present 'Share Capital' in the Balance Sheet of the company as per Schedule III Part I of the Companies Act, 2013. Also prepare Notes to accounts for the same.

SOLUTION :

Scooters India Ltd.

EXTRACT OF BALANCE SHEET *as at* ....

Particulars	Note No.	Current year	Previous year
		₹	₹
EQUITY & LIABILITIES :			
Shareholders Funds :			
(*a*) Share Capital	1	10,00,000	

Notes to Accounts :

	Particulars	₹
(1)	**Share Capital :**	
	Authorised Capital : 5,00,000 Equity Shares of ₹10 each	50,00,000
	Issued Capital : 1,00,000 Equity Shares of ₹10 each	10,00,000
	Subscribed and Fully Paid Capital : 1,00,000 Equity Shares of ₹10 each fully called up	10,00,000

ILLUSTRATION 26.

On 1st April, 2021, Vishwas Ltd. was formed with an authorized capital of ₹10,00,000 divided into 1,00,000 equity shares of ₹10 each. The company issued prospectus inviting applications for 90,000 equity shares. The company received applications for 85,000 equity shares. During the first year, ₹8 per share were called. Ram holding 1,000 shares and Shyam holding 2,000 shares did not pay the first call of

₹2 per share. Shyam's shares were forfeited after the first call and later on 1,500 of the forfeited shares were re-issued at ₹6 per share, ₹8 called up.

Show the following :

(*a*) Share capital in the Balance Sheet of the company as per Schedule-III Part-I of the Companies Act, 2013.

(*b*) Also prepare 'Notes to Accounts' for the same.

SOLUTION : **Extract of Balance Sheet of Vishwas Ltd.**

as at 31st March, 2022

Particulars	*Note No.*	*31st March, 2020*	*31st March, 2019*
		₹	₹
I. EQUITY & LIABILITIES :			
(1) Shareholders Funds :			
(*a*) Share Capital	1	6,77,000	

Notes to Accounts :

	Particulars		₹
(1)	Share Capital :		
	Authorised Share Capital :		
	1,00,000 equity shares of ₹10 each		10,00,000
	Issued Share Capital :		
	90,000 equity shares of ₹10 each		9,00,000
	Subscribed but not fully paid Capital :		
	84,500 equity shares of ₹10 each, ₹8 called up	6,76,000	
	Less : Calls in arrears (1,000 × ₹2)	2,000	
		6,74,000	
	Add : Share forfeiture A/c	3,000	6,77,000

ILLUSTRATION 27.

A holds 100 shares of ₹10 each, on which he has paid only ₹2.50 per share as application money.

B, who holds 200 shares of ₹10 each, has paid ₹2.50 and ₹2 per share as application and allotment money, respectively.

C holds 300 shares of ₹10 each and has paid ₹2.50 per share on application, ₹2 per share on allotment and ₹3 per share on first call.

They failed to pay their arrears and the final call. Therefore the Directors forfeited their shares.

These shares were subsequently reissued for cash at a discount of 10 per cent.

Record journal entries in the books of the company to give effect to the above.

SOLUTION :

CALCULATION TABLE

	Application *₹2.50*	*Allotment* *₹2.00*	*First Call* *₹3.00*	*Final Call* *₹2.50*
A 100 Shares	250	*200	*300	*250
B 200 Shares	500	400	*600	*500
C 300 Shares	750	600	900	*750
Amount Received	1,500	1,000	900	—
Amount not Received	—	200	900	1,500

* Represents amount not received.

JOURNAL ENTRIES

Date	*Particulars*		*L.F.*	*Dr.*	*Cr.*
				₹	₹
	Share Capital A/c	Dr.		6,000	
	To Calls in Arrears A/c(1)				2,600
	To Share Forfeiture A/c				3,400
	(600 shares forfeited)				
	Bank A/c	Dr.		5,400	
	Share Forfeiture A/c	Dr.		600	
	To Share Capital A/c				6,000
	(600 shares of ₹10 each re-issued at a discount of 10%)				
	Share Forfeiture A/c	Dr.		2,800	
	To Capital Reserve A/c				2,800
	(Transfer of the balance of Forfeiture A/c to Capital Reserve A/c)				

Note : (1) Allotment ₹200 + First Call ₹900 + Final Call ₹1,500 = ₹2,600

ILLUSTRATION 28.

Pass journal entries for the forfeiture and re-issue in the following cases :

(*i*) *A* Ltd. forfeited 400 shares of Anil of ₹10 each fully called up for non-payment of final call of ₹2 per share and re-issued to Sunil as fully paid for ₹10 per share.

(*ii*) *B* Ltd. forfeited 500 shares of ₹10 each fully called up for non-payment of first call of ₹2 per share and final call of ₹2 per share. All of these shares were re-issued as fully paid for ₹8 per share.

(*iii*) *C* Ltd. forfeited 600 shares of ₹10 each fully called up for non-payment of allotment money of ₹3 per share, first call of ₹2 per share and final call of ₹2 per share. 400 of these shares were re-issued at ₹9 per share, fully paid up.

(*iv*) *D* Ltd. forfeited 800 shares of ₹10 each fully called up, on which the holder has paid only the application money of ₹3 per share. Out of these, 500 shares were re-issued at ₹11 per share, fully paid up.

SOLUTION :

JOURNAL

Date	Particulars		L.F.	Dr. ₹	Cr. ₹
Case (*i*)	Share Capital A/c	Dr.		4,000	
	To Calls in Arrears A/c				800
	To Share Forfeiture A/c				3,200
	(Forfeiture of 400 shares for non-payment of final call of ₹2 per share)				
	Bank A/c	Dr.		4,000	
	To Share Capital A/c				4,000
	(Re-issue of 400 shares @ ₹10 per share)				
	Share Forfeiture A/c	Dr.		3,200	
	To Capital Reserve A/c				3,200
	(Profit on forfeiture transferred to Capital Reserve A/c)				
Case (*ii*)	Share Capital A/c	Dr.		5,000	
	To Calls in Arrears A/c				2,000
	To Share Forfeiture A/c				3,000
	(Forfeiture of 500 shares for non payment of first call of ₹2 and final call of ₹2 per share				
	Bank A/c	Dr.		4,000	
	Share Forfeiture A/c	Dr.		1,000	
	To Share Capital A/c				5,000
	(Re-issue of 500 shares @ ₹8 per share)				
	Share Forfeiture A/c	Dr.		2,000	
	To Capital Reserve A/c				2,000
	(Balance left in Share Forfeiture A/c, *i.e.*, ₹3,000 – ₹1,000 = ₹2,000 transferred to Capital Reserve A/c)				
Case (*iii*)	Share Capital A/c	Dr.		6,000	
	To Calls in Arrears A/c				4,200
	To Share Forfeiture A/c				1,800
	(Forfeiture of 600 shares for non payment of allotment ₹3, first call ₹2 and final call ₹2 per share)				
	Bank A/c	Dr.		3,600	
	Share Forfeiture A/c	Dr.		400	
	To Share Capital A/c				4,000
	(Re-issue of 400 shares @ ₹9 per share)				
	Share Forfeiture A/c(1)	Dr.		800	
	To Capital Reserve A/c				800
	(Profit on 400 re-issued shares transferred to Capital Reserve A/c)				
Case (*iv*)	Share Capital A/c	Dr.		8,000	
	To Calls in Arrears A/c				5,600
	To Share Forfeiture A/c				2,400
	(Forfeiture of 800 shares)				

	Bank A/c Dr.		5,500	
	To Share Capital A/c			5,000
	To Securities Premium Reserve A/c			500
	(Re-issue of 500 shares @ ₹11 per share)			
	Share Forfeiture A/c[2] Dr.		1,500	
	To Capital Reserve A/c			1,500
	(Gain on 500 re-issued shares transferred to Capital Reserve A/c)			

Notes : (1) Forfeited amount on 600 shares = ₹1,800 ₹

Hence, Forfeited amount on 400 re-issued shares = $\frac{1,800}{600} \times 400$ = 1,200

Less : Loss on re-issue : 400 shares × ₹1 = 400

Transferred to Capital Reserve 800

(2) Forfeited amount on 800 shares = ₹2,400

Hence, Forfeited amount on 500 re-issued shares = $\frac{2,400}{800} \times 500$ = 1,500

ILLUSTRATION 29.

Pass journal entries for the Forfeiture and Re-issue in the following cases :

(*a*) *X* Ltd. forfeited 200 shares of Ravi of ₹10 each ₹8 called up, on which he had paid application and allotment money of ₹3 per share. Out of these, 100 shares were re-issued as fully paid up for ₹8 per share.

(*b*) *Y* Ltd. forfeited 300 shares of ₹10 each, ₹7 called up, for non-payment of First Call of ₹2 per share. Out of these, 100 shares were immediately re-issued at ₹6 per share.

(*c*) *Z* Ltd. forfeited 600 shares of ₹10 each, on which first call of ₹3 per share was not received; the second and final call of ₹2 per share has not yet been called. Out of these, 200 shares were re-issued as ₹8 paid-up for ₹7 per share.

SOLUTION :

JOURNAL

Date	*Particulars*	*L.F.*	*Dr.*	*Cr.*
			₹	₹
(*a*)	Share Capital A/c (200 Shares × ₹8) Dr.		1,600	
	To Calls in Arrear A/c (200 × ₹5)			1,000
	To Share Forfeiture A/c (200 × ₹3)			600
	(Forfeiture of 200 shares of Ravi)			
	Bank A/c Dr.		800	
	Share Forfeiture A/c Dr.		200	
	To Share Capital A/c			1,000
	(Re-issue of 100 shares @ ₹8 per share fully paid)			
	Share Forfeiture A/c[1] Dr.		100	
	To Capital Reserve A/c			100
	(Gain on 100 re-issued shares transferred to Capital Reserve)			

(b)	Share Capital A/c (300 Shares × ₹7)	Dr.		2,100	
	To Calls in Arrears A/c (300 × ₹2)				600
	To Share Forfeiture A/c (300 × ₹5)				1,500
	(Forfeiture of 300 shares)				
	Bank A/c	Dr.		600	
	Share Forfeiture A/c	Dr		100	
	To Share Capital A/c				700
	(Re-issue of 100 shares at ₹6 per share; Loss of ₹1 per share (*i.e.*, ₹7 called up — ₹6) debited to Forfeiture A/c)				
	Share Forfeiture A/c(2)	Dr.		400	
	To Capital Reserve A/c				400
	(Gain on 100 re-issued shares transferred to Capital Reserve A/c)				
(c)	Share Capital A/c (600 Shares × ₹8)	Dr.		4,800	
	To Calls in Arrears A/c (600 Shares × ₹3)				1,800
	To Share Forfeiture A/c (600 Shares × ₹5)				3,000
	(Forfeiture of 600 shares)				
	Bank A/c	Dr.		1,400	
	Share Forfeiture A/c	Dr.		200	
	To Share Capital A/c				1,600
	(Re-issue of 200 shares at ₹7 per share, loss of ₹1 per share (*i.e.*, ₹8 called up – ₹7) debited to Forfeiture A/c)				
	Share Forfeiture A/c(3)	Dr.		800	
	To Capital Reserve A/c				800
	(Gain on 200 re-issued shares transferred to Capital Reserve A/c)				

Notes : (1) Forfeited amount on 200 shares = ₹600 ₹

Hence, Forfeited amount on 100 shares $= \frac{600}{200} \times 100$ = 300

Less : Loss on Re-issue : 100 shares × ₹2 = 200

Transferred to Capital Reserve = 100

(2) Forfeited amount on 300 shares = ₹1,500

Hence, Forfeited amount on 100 shares $= \frac{1,500}{300} \times 100$ = 500

Less : Loss on Re-issue: 100 shares × ₹1 = 100

Transferred to Capital Reserve = 400

(3) Forfeited amount on 600 shares = ₹3,000

Hence, Forfeited amount on 200 shares $= \frac{3,000}{600} \times 200$ = 1,000

Less : Loss on Re-issue : 200 shares × ₹1 = 200

Transferred to Capital Reserve = 800

ILLUSTRATION 30.

(*a*) Ravi Ltd., forfeited 800 shares of ₹10 each, ₹7.50 paid, for non-payment of Final Call of ₹2.50 per share. Out of these, 600 shares were re-issued as fully paid up in such a way that ₹2,100 were transferred to capital reserve. Pass necessary journal entries.

(*b*) *X* Ltd., forfeited 800 shares of ₹10 each, ₹7.50 called-up, for non-payment of First Call of ₹2.50 per share. Out of these, 600 shares were re-issued for ₹6 per share as ₹7.50 paid up. Pass necessary journal entries.

(*c*) 400 shares of ₹10, on which ₹8 has been called and ₹6 has been paid, are forfeited. Out of these, 300 are re-issued for ₹7 as fully paid. Give journal entries.

SOLUTION : (*a*)

JOURNAL

Date	*Particulars*		*L.F.*	*Dr.* ₹	*Cr.* ₹
	Share Capital A/c (800 × ₹10)	Dr.		8,000	
	To Calls in Arrears A/c (800 × ₹2.50)				2,000
	To Share Forfeiture A/c (800 × ₹7.50)				6,000
	(Forfeiture of 800 shares)				
	Bank A/c[(1)]	Dr.		3,600	
	Share Forfeiture A/c	Dr.		2,400	
	To Share Capital A/c				6,000
	(Re-issue of 600 shares @ ₹6 per share as fully paid up)				
	Share Forfeiture A/c	Dr.		2,100	
	To Capital Reserve A/c				2,100
	(Gain on 600 re-issued shares transferred to Capital Reserve)				

Note : (1) Forfeited amount on 800 shares = ₹6,000 ₹

∴ Forfeited amount on 600 shares $= \frac{6,000}{800} \times 600 = 4,500$

Less : Transferred to Capital Reserve = 2,100

Loss on Re-issue 2,400

Per Share Loss on Re-issue $= \frac{2,400}{600} =$ ₹4 per share

Hence, Shares are reissued at ₹10 – ₹4 = ₹6 per share

(*b*)

JOURNAL

Date	*Particulars*		*L.F.*	*Dr.* ₹	*Cr.* ₹
	Share Capital A/c (800 × ₹7.50)	Dr.		6,000	
	To Calls in Arrears A/c (800 × ₹2.50)				2,000
	To Share Forfeiture A/c (800 × ₹5)				4,000
	(Forfeiture of 800 shares)				

	Bank A/c	Dr.		3,600	
	Share Forfeiture A/c	Dr.		900	
	To Share Capital A/c				4,500
	(Re-issue of 600 shares @ ₹6 per share as ₹7.50 paid up)				
	Share Forfeiture A/c[(2)]	Dr.		2,100	
	To Capital Reserve A/c				2,100
	(Gain on 600 re-issued shares transferred to Capital Reserve)				

Note : (2) Forfeited amount on 800 shares = ₹4,000 ₹

∴ Forfeited amount on 600 shares = ₹4,000 × $\frac{600}{800}$ = 3,000

Less : Loss on re-issue of 600 shares @ ₹1.50 each = 900

2,100

(*c*) JOURNAL

Date	*Particulars*		*L.F.*	*Dr.*	*Cr*
				₹	₹
	Share Capital A/c	Dr.		3,200	
	To Calls in Arrears A/c				800
	To Share Forfeiture A/c				2,400
	(Forfeiture of 400 shares)				
	Bank A/c	Dr.		2,100	
	Share Forfeiture A/c	Dr.		900	
	To Share Capital A/c				3,000
	(Re-issue of 300 shares at ₹7 as fully paid)				
	Share Forfeiture A/c[(3)]	Dr.		900	
	To Capital Reserve A/c				900
	(Gain on re-issue of 300 shares transferred to Capital Reserve)				

Note : (3) Forfeited amount on 400 shares = ₹2,400 ₹

∴ Forfeited amount on 300 shares = ₹2,400 × $\frac{300}{400}$ = 1,800

Less : Loss on re-issue of 300 shares @ ₹3 each = 900

900

Forfeiture of Shares Issued at Premium

In such cases there may be two situations :

(*i*) When premium on forfeited shares became due but is not received.

(*ii*) When premium on forfeited shares is received.

(*i*) When Premium on Forfeited Shares became due but is not Received

ILLUSTRATION 31.

During the year 2014-15, *ABC* Ltd. issued 10,000 Equity Shares of ₹50 each at ₹55 per share, payable as follows :

On Application ₹15

On Allotment	₹20 (including premium ₹5)
On 1st and Final Call	₹20

All the issued shares were subscribed for by the public.

One shareholder holding 500 shares did not pay the amount due on allotment and his shares were immediately forfeited.

Another shareholder holding 100 shares paid the amount of the 1st and Final Call with allotment.

After the company had made the 1st and Final Call, 200 of the forfeited shares were reissued as fully called up at ₹45 per share.

The share issue expenses were ₹7,000 which were written off at the end of the year.

You are required to pass journal entries in the books of the company for the year ending 31st March, 2015. Also prepare the Opening Balance Sheet. *(I.S.C. 2016)*

SOLUTION : JOURNAL OF ABC LTD.

Date	*Particulars*		*L.F.*	*Dr. (₹)*	*Cr. (₹)*
	Bank A/c	Dr.		1,50,000	
	To Share Application A/c				1,50,000
	(Share application money received)				
	Share Application A/c	Dr.		1,50,000	
	To Equity Share Capital A/c				1,50,000
	(Share application transferred to share capital)				
	Share Allotment A/c	Dr.		2,00,000	
	To Equity Share Capital A/c				1,50,000
	To Securities Premium Reserve A/c				50,000
	(Share allotment due)				
	Bank A/c	Dr.		1,92,000	
	Calls-in-Arrears A/c	Dr.		10,000	
	To Share Allotment A/c				2,00,000
	To Calls-in-Advance A/c				2,000
	(Share allotment received)				
	Equity Share Capital A/c	Dr.		15,000	
	Securities Premium Reserve A/c	Dr.		2,500	
	To Share Forfeited A/c				7,500
	To Calls-in-Arrears A/c				10,000
	(500 shares forfeited)				
	Share 1st & Final Call A/c	Dr.		1,90,000	
	To Equity Share Capital A/c				1,90,000
	(1st and Final Call due on 9,500 shares)				
	Bank A/c	Dr.		1,88,000	
	Calls-in-Advance A/c	Dr.		2,000	
	To Share 1st & Final Call A/c				1,90,000
	(Share 1st and final call received)				

Particulars			Debit	Credit
Bank A/c	Dr.		9,000	
Share Forfeited A/c	Dr.		1,000	
To Equity Share Capital A/c				10,000
(200 forfeited shares reissued)				
Share Forfeited A/c$^{(1)}$	Dr.		2,000	
To Capital Reserve A/c				2,000
(Gain on reissue of 200 forfeited shares transferred to Capital Reserve)				
Share Issue Expenses A/c	Dr.		7,000	
To Bank A/c				7,000
(Share issue expenses)				
Securities Premium Reserve A/c	Dr.		7,000	
To Share Issue Expenses A/c				7,000
(Share issue expenses written off)				

			₹
Note : (1)	Forfeited amount on 500 shares	$= 7{,}500$	
	Hence, Forfeited amount on 200 shares	$= \frac{7{,}500}{500} \times 200 =$	3,000
	Less : Loss on Reissue		1,000
	Transferred to Capital Reserve		2,000

BALANCE SHEET OF *ABC* LTD.

as at 31st March, 2015

Particulars	*Note No.*	*Current year*	*Previous year*
		₹	₹
I. EQUITY AND LIABILITIES :			
Shareholder's Funds :			
(*a*) Share Capital	1	4,89,500	
(*b*) Reserve and Surplus	2	42,500	
		5,32,000	
II. ASSETS :			
Current Assets :			
Cash and Bank Balance	3	5,32,000	

Notes to Accounts :

		₹	₹
(1) **Share Capital :**			
Authorised*			
.... Shares of ₹ .... each		....	
Issued :			
10,000 shares of ₹50 each		5,00,000	
Subscribed and Fully Paid Capital :			
9,700 shares of ₹50 each fully paid	4,85,000		

Add : Share Forfeited A/c	4.500	4.89.500	
(2) **Reserves & Surplus :**			
Capital Reserve		2.000	
Securities Premium Reserve		40.500	
		42.500	
(3) **Cash and Bank Balance :**			
Cash at Bank		5,32,000	

*As per ISC Guidelines, Authorised Capital has to be shown in notes to accounts even if it is not given in the question.

(*ii*) When Premium on Forfeited Shares is Received

ILLUSTRATION 12.

Kamal Ltd., was formed for the purpose of purchasing Rajesh Ltd. and was registered with a nominal capital of ₹2,00,000 divided into 2,000 equity shares of ₹100 each. 1,000 shares were issued as fully paid to the vendors in payment of the purchase consideration. The remaining 1,000 shares were offered for public subscription at a premium of ₹5 per share payable as under : On Application ₹30 per Share; On Allotment ₹25 per Share (including premium); On First Call ₹20 per Share and on Final Call ₹30 per share.

Applications were received for 900 shares which were duly allotted, and the allotment money was duly received. At the time of the first call, a shareholder who held 100 shares failed to pay the first call money and his shares were forfeited. These shares were re-issued at ₹60 per share, ₹70 per share paid. Final call has not been made.

You are required to (*i*) give necessary journal entries to record the above transactions, and (*ii*) show how share capital would appear in the Balance Sheet of the Company.

SOLUTION :

In the Books of Kamal Ltd.

Date	*Particulars*		*L.F.*	*Dr.*	*Cr.*
				₹	₹
	Sundry Assets A/c	Dr.		1,00,000	
	To Rajesh Ltd.				1,00,000
	(Assets purchased from Rajesh Ltd.)				
	Rajesh Ltd.	Dr.		1,00,000	
	To Equity Share Capital A/c				1,00,000
	(1,000 shares of ₹100 each issued to vendors)				
	Bank A/c	Dr.		27,000	
	To Equity Share Application A/c				27,000
	(Application money received on 900 equity shares @ ₹30 each)				

Equity Share Application A/c	Dr.	27,000	
To Equity Share Capital A/c			27,000
(Equity share application money transferred to Equity Share Capital A/c)			
Equity Share Allotment A/c	Dr.	22,500	
To Equity Share Capital A/c			18,000
To Securities Premium Reserve A/c			4,500
(Allotment money due)			
Bank A/c	Dr.	22,500	
To Equity Share Allotment A/c			22,500
(Allotment money received)			
Equity Share First Call A/c	Dr.	18,000	
To Equity Share Capital A/c			18,000
(First call due on 900 equity shares @ ₹20 per share)			
Bank A/c	Dr.	16,000	
Calls in Arrears A/c	Dr.	2,000	
To Equity Share First Call A/c			18,000
(First call money received on 800 equity shares @ ₹20 each)			
Equity Share Capital A/c(1)	Dr.	7,000	
To Calls in Arrears A/c			2,000
To Share Forfeiture A/c			5,000
(100 equity shares forfeited, ₹70 per share called up, due to non-payment of first call of ₹20 per share)			
Bank A/c	Dr.	6,000	
Share Forfeiture A/c	Dr.	1,000	
To Equity Share Capital A/c			7,000
(100 equity shares re-issued at ₹60 per share, ₹70 per share called up)			
Share Forfeiture A/c	Dr.	4,000	
To Capital Reserve A/c			4,000
(Balance of Forfeiture A/c transferred to Capital Reserve A/c)			

EXTRACT OF BALANCE SHEET OF KAMAL LTD.

as at ....

Particulars	*Note No.*	*Current year*	*Previous year*
I. EQUITY AND LIABILITIES :		₹	₹
Shareholder's Funds :			
(*a*) Share Capital	1	1,63,000	

Notes to Accounts :

	₹	₹
(1) Share Capital :		
Authorised Capital :		
2,000 Equity Shares of ₹100 each	2,00,000	
Issued Capital :		
2,000 Equity Shares of ₹100 each	2,00,000	
Subscribed and Fully Paid Capital :		
1,000 Shares of ₹100 each fully paid issued for consideration other than cash	1,00,000	
Subscribed but not Fully Paid Capital :		
900 Shares of ₹100 each ₹70 called	63,000	
	1,63,000	

Note : Securities Premium Reserve A/c will not be debited in the entry for the forfeiture of shares, because premium is due with the allotment and allotment money has been received in full.

ILLUSTRATION 33.

Pioneer Ltd. invited applications for 12,000 shares of ₹100 each to be issued at a premium of 10% payable as follows :

On Application	₹25
On Allotment	₹40
On First & Final Call	₹35

Applications were received for 10,000 shares and all of these were accepted. All the money due was received except the first and final call on 100 shares which were forfeited. 60 of these forfeited shares were reissued @ ₹90 per share credited as fully paid.

You are required to :

(*a*) Pass the necessary Journal Entries.

(*b*) Prepare the Balance Sheet of the company. *(I.S.C. 2007)*

SOLUTION :

Total of 25 + 40 + 35 amounts to ₹100. Since it is not mentioned in the question as to when the premium is receivable, it will be assumed that the premium is due alongwith allotment money. Hence, amount due on allotment will be ₹50 (including premium of ₹10).

JOURNAL OF PIONEER LTD.

Date	*Particulars*		*L.F.*	*Dr.*	*Cr.*
				₹	₹
	Bank A/c	Dr.		2,50,000	
	To Share Application A/c				2,50,000
	(Application money received on 10,000 shares @ ₹25 each)				

Share Application A/c	Dr.		2,50,000	
Share Capital A/c				2,50,000
(Share application money transferred to Share Capital A/c)				
Share Allotment A/c	Dr.		5,00,000	
To Share Capital A/c				4,00,000
To Securities Premium Reserve A/c				1,00,000
(Allotment money due)				
Bank A/c	Dr.		5,00,000	
To Share Allotment A/c				5,00,000
(Allotment money received)				
Share First & Final Call A/c	Dr.		3,50,000	
To Share Capital A/c				3,50,000
(First & Final Call due on 10,000 shares @ ₹35 per share)				
Bank A/c	Dr.		3,46,500	
Calls in Arrears A/c	Dr.		3,500	
To Share First & Final Call A/c				3,50,000
(First & Final call money received on 9,900 shares @ ₹35 each)				
Share Capital A/c	Dr.		10,000	
To Calls in Arrears A/c				3,500
To Share Forfeiture A/c				6,500
(100 shares forfeited, due to non-payment of first & final call of ₹35 per share)				
Bank A/c	Dr.		5,400	
Share Forfeiture A/c	Dr.		600	
To Share Capital A/c				6,000
(60 shares re-issued at ₹90 per share, as fully paid)				
Share Forfeiture A/c	Dr.		3,300	
To Capital Reserve A/c(4)				3,300
(Gain on Forfeiture transferred to Capital Reserve A/c)				

BALANCE SHEET OF PIONEER LTD.

as at ....

Particulars	*Note No.*	*Current year*	*Previous year*
I. EQUITY AND LIABILITIES :		₹	₹
Shareholder's Funds :			
(*a*) Share Capital	1	9,98,600	
(*b*) Reserve and Surplus	2	1,03,300	
		11,01,900	
II. ASSETS :			
Current Assets :			
Cash and Bank Balance	3	11,01,900	

Notes to Accounts :

		₹	₹
(1) **Share Capital**			
Authorised Capital :			
……….. Shares of ₹100 each		…………	
Issued Capital			
12,000 Shares of ₹100 each		12,00,000	
Subscribed & Fully Paid Capital :			
9,960 Shares of ₹100 each	9,96,000		
Add : Share Forfeiture A/c(6)	2,600	9,98,600	
(2) **Reserve and Surplus :**			
Capital Reserve A/c		3,300	
Securities Premium Reserve A/c		1,00,000	
		1,03,300	
(3) **Cash and Bank Balance :**			
Cash at Bank		11,01,900	

(4) Forfeited amount on 100 shares = 6,500 ₹

Hence, Forfeited amount on 60 shares = $\frac{6,500}{100} \times 60$ = 3,900

Less : Loss on Re-issue 600

Amount Transferred to Capital Reserve 3,300

(5) Students are advised to prepare a Bank A/c in order to ascertain the balance of Cash at bank.

(6) Forfeited amount on 40 unissued shares : $\frac{6,500}{100} \times 40$ = ₹2,600.

ILLUSTRATION 34.

Give journal entries for forfeiture and re-issue of shares :

(*i*) *A* Ltd. forfeited 1,000 shares of ₹10 each, ₹7 called up, issued at a premium of 20% (to be paid at the time of allotment) for non-payment of a first call of ₹2 per share. Out of these, 600 shares were re-issued as ₹7 paid up for ₹4 per share.

(*ii*) *B* Ltd. forfeited 1,000 shares of ₹10 each, ₹7 called up, issued at a premium of 20% (to be paid at the time of allotment) for non-payment of allotment money of ₹4 per share (including premium) and first call of ₹2 per share. Out of these, 600 shares were re-issued as fully paid in such a way that ₹900 were transferred to capital reserve.

SOLUTION : (i) JOURNAL OF *A* LTD.

Date	Particulars	L.F.	Dr.	Cr.
			₹	₹
	Share Capital A/c Dr.		7,000	
	To Calls in Arrears A/c			2,000
	To Share Forfeiture A/c			5,000
	(Forfeiture of 1,000 shares)			
	Bank A/c Dr.		2,400	
	Share Forfeiture A/c Dr.		1,800	
	To Share Capital A/c			4,200
	(Re-issue of 600 shares @ ₹4 each)			
	Share Forfeiture A/c(1) Dr.		1,200	
	To Capital Reserve A/c			1,200
	(Gain on 600 re-issued shares transferred to Capital Reserve)			

Note : (1) As Forfeited amount on 1,000 shares = ₹5,000 ₹

Therefore, Forfeited amount on 600 shares = ₹$\frac{5,000}{1,000} \times 600$ = 3,000

Less : Loss on re-issue = 1,800

Transferred to Capital Reserve 1,200

(ii) JOURNAL OF *B* LTD.

Date	Particulars	L.F.	Dr.	Cr.
			₹	₹
	Share Capital A/c Dr.		7,000	
	Securities Premium Reserve A/c Dr.		2,000	
	To Calls in Arrears A/c			6,000
	To Share Forfeiture A/c			3,000
	(Forfeiture of 1,000 shares)			
	Bank A/c(2) Dr.		5,100	
	Share Forfeiture A/c Dr.		900	
	To Share Capital A/c			6,000
	(Re-issue of 600 shares @ ₹8.50 each)			
	Share Forfeiture A/c Dr.		900	
	To Capital Reserve A/c			900
	(Gain on 600 re-issued shares transferred to Capital Reserve)			

Note : (2) As Forfeited amount on 1,000 shares = ₹3,000 ₹

Therefore, Forfeited amount on 600 shares = ₹$\frac{3,000}{1,000} \times 600$ = 1,800

Less : Transferred to Capital Reserve = 900

Loss on Re-issue 900

Per Share Loss on Re-issue = $\frac{\text{₹}900}{600}$ = ₹1.50 per share

Hence, Shares are reissued at ₹10 – ₹1.50 = ₹8.50 per share

ILLUSTRATION 35.

Give journal entries for forfeiture and re-issue of shares :

(*i*) *C* Ltd. forfeited 800 shares of ₹10 each, issued at 30% premium (to be paid at the time of allotment) for non-payment of a first call of ₹2 per share. The second and final call of ₹2 has not yet been called. Out of these, 200 shares were re-issued as ₹8 paid up for ₹8 per share.

(*ii*) *D* Ltd. forfeited, 800 shares of ₹10 each, issued at 30% premium for non-payment of allotment money of ₹5 per share (including premium) and first call of ₹2 per share. The second and final call of ₹2 has not yet been called. Out of these, 200 shares were re-issued as fully paid up for ₹11 per share.

SOLUTION : (i) JOURNAL OF *C* LTD.

Date	*Particulars*		*L.F.*	*Dr.*	*Cr.*
				₹	₹
	Share Capital A/c	Dr.		6,400	
	To Calls in Arrears A/c				1,600
	To Share Forfeiture A/c				4,800
	(Forfeiture of 800 shares)				
	Bank A/c	Dr.		1,600	
	To Share Capital A/c				1,600
	(Re-issue of 200 shares @ ₹8 each)				
	Share Forfeiture A/c(1)	Dr.		1,200	
	To Capital Reserve A/c				1,200
	(Gain on 200 re-issued shares transferred to Capital Reserve)				

Note : (1) As Forfeited amount on 800 shares = ₹4,800

Therefore, Forfeited amount on 200 shares = ₹$\frac{4{,}800}{800}$ × 200 = ₹1,200

Since there is no loss on re-issue, the full amount of ₹1,200 will be transferred to Capital Reserve.

(ii) JOURNAL OF *D* LTD.

Date	*Particulars*		*L.F.*	₹	₹
	Share Capital A/c	Dr.		6,400	
	Securities Premium A/c	Dr.		2,400	
	To Calls in Arrears A/c				5,600
	To Share Forfeiture A/c				3,200
	(Forfeiture of 800 shares)				
	Bank A/c	Dr.		2,200	
	To Share Capital A/c				2,000
	To Securities Premium Reserve A/c				200
	(Re-issue of 200 shares @ ₹11 each)				

	Share Forfeiture A/c(2) Dr.		800	
	To Capital Reserve A/c			800
	(Gain on 200 re-issued shares transferred to Capital Reserve)			

Note : (2) As Forfeited amount on 800 shares = ₹3,200

Therefore, Forfeited amount on 200 shares = $₹\frac{3,200}{800} \times 200$ = ₹800

Since there is no loss on re-issue, the full amount of ₹800 will be transferred to Capital Reserve.

ILLUSTRATION 36.

X Ltd. issued 60,000 shares of ₹10 each at a premium of 20% payable as follows: On Application ₹5 (including premium); On Allotment ₹3; and On First and Final Call ₹4.

The company received applications for 75,000 shares and allotment was made as follows :

List I Applicants for 40,000 shares were allotted in full.
List II Applicants for 25,000 shares were allotted 20,000 shares.
List III Applicants for 10,000 shares were allotted Nil shares.

A shareholder to whom 200 shares were allotted under List I paid full amount due on shares alongwith allotment money. Another shareholder holding 600 shares failed to pay the amount due on call. His shares were forfeited and 500 of these shares were subsequently re-issued as fully paid @ ₹11 per share.

Expenses of issue came to ₹20,000 which were fully written off against securities premium a/c.

Pass journal entries and give balance sheet of the company.

SOLUTION :

JOURNAL OF *X* LTD.

Date	*Particulars*	*L.F.*	*Dr.*	*Cr.*
			₹	₹
	Bank A/c Dr.		3,75,000	
	To Share Application A/c			3,75,000
	(Application money received on 75,000 shares)			
	Share Application A/c Dr.		3,75,000	
	To Share Capital A/c			1,80,000
	To Securities Premium Reserve A/c			1,20,000
	To Share Allotment A/c			25,000
	To Bank A/c			50,000
	(Application money transferred)			
	Share Allotment A/c Dr.		1,80,000	
	To Share Capital A/c			1,80,000
	(Allotment due on 60,000 shares @ ₹3 per share)			
	Bank A/c Dr.		1,55,800	
	To Share Allotment A/c			1,55,000
	To Calls in Advance A/c			800

	(Receipt of allotment money : 60,000 shares @ ₹3 1,80,000 *Less* : Already received alongwith applications 25,000 1,55,000 *Add* : Received in advance on 200 shares @ ₹4 800 1,55,800)			
	Share First & Final Call A/c Dr. To Share Capital A/c (First & final call due on 60,000 shares @ ₹4 per share)		2,40,000	 2,40,000
	Bank A/c Dr. Calls in Advance A/c Dr. Calls in Arrears A/c Dr. To Share First & Final Call A/c (Receipt of first & final call except on 600 shares @ ₹4)		2,36,800 800 2,400	 2,40,000
	Share Capital A/c Dr. To Calls in Arrears A/c To Share Forfeiture A/c (Forfeiture of 600 shares for non-payment of first & final call)		6,000	 2,400 3,600
	Bank A/c Dr. To Share Capital A/c To Securities Premium Reserve A/c (Re-issue of 500 shares @ ₹11 per share)		5,500	 5,000 500
	Share Forfeiture A/c Dr. To Capital Reserve A/c (Gain on 500 re-issued shares transferred to capital reserve)		3,000(4)	 3,000
	Share Issue Expenses A/c Dr. To Bank A/c (Expenses incurred on issue of shares)		20,000	 20,000
	Securities Premium Reserve A/c Dr. To Share Issue Expenses A/c (Share issue expenses written off against Securities premium reserve)		20,000	 20,000

BALANCE SHEET OF *X* LTD.

as at ....

Particulars	*Note No.*	*Current year*	*Previous year*
I. EQUITY AND LIABILITIES :		₹	₹
Shareholder's Funds :			
(*a*) Share Capital	1	5,99,600	

(*b*) Reserve and Surplus	2	1,03,500	
		7,03,100	
II. ASSETS :			
Current Assets :			
Cash and Bank Balance(6)	3	7,03,100	

Notes to Accounts :

		₹	₹
(1) **Share Capital :**			
Authorised :			
.... Shares of ₹ .... each		....	
Issued :			
60,000 shares of ₹10 each fully paid		6,00,000	
Subscribed and Fully Paid Capital :			
59,900 shares of ₹10 each fully paid	5,99,000		
Add : Share Forfeiture A/c	600(5)	5,99,600	
(2) **Reserves and Surplus :**			
Capital Reserve A/c		3,000	
Securities Premium Reserve A/c		1,00,500	
		1,03,500	
(3) **Cash and Bank Balance :**			
Cash at Bank		7,03,100	

Note (4) : Forfeited amount on 600 shares = ₹3,600

Hence, Forfeited amount on 500 shares $= ₹\frac{3,600}{600} \times 500 = ₹3,000$

Note (5) : Forfeited amount on the forfeiture of 600 shares is ₹3,600. Out of this amount, forfeited amount on the re-issue of 500 shares ₹3,000 has been transferred to capital reserve. The balance of ₹600 will be shown on the equity and liabilities side of the balance sheet under the head 'Share Capital'.

Note (6) : Students are advised to prepare a Bank A/c in order to ascertain the balance of cash at bank.

ILLUSTRATION 37.

S Ltd. offers 1,00,000 equity shares of ₹10 each payable ₹3 on application, ₹3 on allotment (including premium ₹2), ₹4 on first call three months after allotment and ₹2 on final call three months after first call. Applications were received for 1,58,500 shares and allotment was made as under :

	Shares allotted
Allotment in full (Mr. *D* paid in full on allotment in respect of 4,000 shares)	19,000
Allotment of 2/3 of shares applied for	80,000
Allotment of 1/2 of shares applied for	1,000

Application money of ₹52,500 in respect of 17,500 shares upon which no allotment was made was returned to applicants. All amounts were received except final call on 100 shares which were forfeited and re-issued later on @ ₹9 each. Interest on calls in advance is paid @ 12% p.a.

Give necessary journal entries.

SOLUTION :

JOURNAL

Date	*Particulars*	*L.F.*	*Dr.*	*Cr.*
			₹	₹
	Bank A/c Dr.		4,75,500	
	To Equity Share Application A/c			4,75,500
	(Application money received on 1,58,500 shares)			
	Equity Share Application A/c Dr.		4,75,500	
	To Equity Share Capital A/c			3,00,000
	To Equity Share Allotment A/c⁽¹⁾			1,23,000
	To Bank A/c			52,500
	(Application money transferred)			
	Equity Share Allotment A/c Dr.		3,00,000	
	To Equity Share Capital A/c			1,00,000
	To Securities Premium Reserve A/c			2,00,000
	(Allotment due on 1,00,000 shares @ ₹3 including premium @ ₹2 per share)			
	Bank A/c Dr.		2,01,000	
	To Equity Share Allotment A/c			1,77,000
	To Calls in Advance A/c⁽²⁾			24,000
	(Allotment money received : 3,00,000			
	Less : Already received alongwith applications 1,23,000			
	1,77,000			
	Add : Received in advance 24,000			
	2,01,000)			
	Equity Share First Call A/c Dr.		4,00,000	
	To Equity Share Capital A/c			4,00,000
	(First Call due on 1,00,000 shares @ ₹4 per share)			
	Bank A/c Dr.		3,84,000	
	Calls in Advance A/c Dr.		16,000	
	To Equity Share First Call A/c			4,00,000
	(First Call money received less ₹16,000 received in advance)			
	Equity Share Final Call A/c Dr.		2,00,000	
	To Equity Share Capital A/c			2,00,000
	(Final Call due on 1,00,000 shares @ ₹2 per share)			

Bank A/c	Dr.	1,91,800	
Calls in Advance A/c	Dr.	8,000	
Calls in Arrears A/c	Dr.	200	
To Equity Share Final Call A/c			2,00,000
(Final Call received, except on 100 shares @ ₹2 per share)			
Equity Share Capital A/c	Dr.	1,000	
To Calls in Arrears A/c			200
To Share Forfeiture A/c			800
(Forfeiture of 100 shares for non-payment of final call)			
Bank A/c	Dr.	900	
Share Forfeiture A/c	Dr.	100	
To Equity Share Capital A/c			1,000
(100 shares re-issued at ₹9 per share)			
Share Forfeiture A/c	Dr.	700	
To Capital Reserve A/c			700
(Transfer of gain on re-issue)			
Interest A/c[(3)]	Dr.	960	
To Bank A/c			960
(Interest paid on calls in advance)			

Working Notes :

(1) Allotment was made as follows :

		Shares Allotted
To the Applicants of	19,000 Shares	19,000
To the Applicants of	1,20,000 Shares	80,000
To the Applicants of	2,000 Shares	1,000
To the Applicants of	17,500 Shares	Nil
	1,58,500	1,00,000

	₹
Total Amount Adjusted on Allotment :	
Applicants for 1,20,000 shares have been allotted 80,000 shares. Hence, excess application money received from them on 40,000 shares @ ₹3 per share	1,20,000
Applicants for 2,000 shares have been allotted 1,000 shares. Hence, excess application money received from them on 1,000 shares @ ₹3 per share = ₹3,000. Whole of this amount will be adjusted on allotment because the amount due on allotment on these 1,000 shares @ ₹3 per share also amounts to ₹3,000	3,000
	1,23,000

(2) Calls in Advance paid by Mr. *D* on his 4,000 shares :

	₹
For Ist Call @ ₹4 per share on 4,000 shares	16,000
For IInd Call @ ₹2 per share on 4,000 shares	8,000
	24,000

(3) Interest on Calls in Advance :		₹
On ₹16,000 for 3 months = $16{,}000 \times \frac{12}{100} \times \frac{3}{12}$	=	480
On ₹8,000 for 6 months = $8{,}000 \times \frac{12}{100} \times \frac{6}{12}$	=	480
		960

ILLUSTRATION 38.

VXN Ltd. invited applications for issuing 50,000 equity shares of ₹10 each at a premium of ₹8 per share. The amount was payable as follows :

On Application	: ₹4 per share (including ₹2 premium)
On Allotment	: ₹6 per share (including ₹3 premium)
On First Call	: ₹5 per share (including ₹1 premium)
On Second and Final Call	: Balance Amount

The issue was fully subscribed. Gopal, a shareholder holding 200 shares, did not pay the allotment money and Madhav, a holder of 400 shares, paid his entire share money along with the allotment money. Gopal's shares were immediately forfeited after allotment. Afterwards, the first call was made. Krishna, a holder of 100 shares, failed to pay the first call money and Girdhar, a holder of 300 shares, paid the second call money also along with the first call. Krishna's shares were forfeited immediately after the first call. Second and final call was made afterwards and was duly received. All the forfeited shares were reissued at ₹9 per share fully paid up.

Pass necessary journal entries for the above transactions in the books of the company. *(C.B.S.E. 2017)*

SOLUTION :

JOURNAL of VZN Ltd.

Date	*Particulars*		*L.F.*	*Dr. (₹)*	*Cr. (₹)*
	Bank A/c	Dr.		2,00,000	
	To Share Application A/c				2,00,000
	(Share Application money received)				
	Share Application A/c	Dr.		2,00,000	
	To Share Capital A/c				1,00,000
	To Securities Premium Reserve A/c				1,00,000
	(Share Application money transferred)				
	Share Allotment A/c	Dr.		3,00,000	
	To Share Capital A/c				1,50,000
	To Securities Premium Reserve A/c				1,50,000
	(Share Allotment money due)				
	Bank A/c (3,00,000 – 1,200 + 3,200)	Dr.		3,02,000	
	Calls in Arrears A/c	Dr.		1,200	
	To Share Allotment A/c				3,00,000
	To Calls in Advance A/c (400 × ₹8)				3,200
	(Share allotment money received alongwith Calls in Advance)				

Share Capital A/c (200 × 5)	Dr.	1,000	
Securities Premium Reserve A/c (200 × 3)	Dr.	600	
To Calls in Arrears A/c			1,200
To Forfeited Shares A/c			400
(Forfeiture of 200 shares held by Gopal)			
Share First Call A/c (49,800 × 5)	Dr.	2,49,000	
To Share Capital A/c (49,800 × 4)			1,99,200
To Securities Premium Reserve A/c (49,800 × 1)			49,800
(First Call due on 49,800 shares)			
Bank A/c (2,49,000 – 500 – 2,000 for calls in advance)	Dr.	2,46,500	
Calls in Advance A/c (400 × 5)	Dr.	2,000	
Calls in Arrears A/c	Dr.	500	
To Share First Call A/c			2,49,000
(First call received on 49,700 shares)			
Bank A/c (300 × 3)	Dr.	900	
To Calls in Advance A/c			900
(Second call received in advance on Girdhar's 300 shares)			
Share Capital A/c (100 × ₹9)	Dr.	900	
Securities Premium Reserve A/c	Dr.	100	
To Calls in Arrears A/c			500
To Forfeited Shares A/c			500
(Forfeiture of 100 shares held by Krishna)			
Share Second & Final Call A/c (49,700 × ₹3)	Dr.	1,49,100	
To Share Capital A/c (49,700 × ₹1)			49,700
To Securities Premium Reserve A/c (49,700 × ₹2)			99,400
(Second & Final Call due on 49,700 shares)			
Bank A/c (1,49,100 – 2,100)	Dr.	1,47,000	
Calls in Advance A/c (700 × ₹3)	Dr.	2,100	
To Share Second & Final Call A/c			1,49,100
(Receipt of Second & Final Call)			
Bank A/c (300 × ₹9)	Dr.	2,700	
Forfeited Shares A/c (300 × ₹1)	Dr.	300	
To Share Capital A/c			3,000
(Re-issue of 300 forfeited shares)			
Forfeited Shares A/c (900 – 300)	Dr.	600	
To Capital Reserve A/c			600
(Gain on re-issue transferred)			

ILLUSTRATION 39.

Give Journal entries to record the following transactions of forfeiture and re-issue of shares and open share forfeited account.

L Ltd. forfeited 470 Equity Shares of ₹10 each issued at a premium of ₹5 per share for non-payment of allotment money of ₹8 per share (including share premium ₹5 per share) and the first and final call of ₹5 per share. Out of these 60 Equity Shares were subsequently re-issued at ₹14 per share.

SOLUTION :

In the Books of *L* Ltd.

JOURNAL

Date	*Particulars*		*L.F.*	*Dr.*	*Cr.*
				₹	₹
	Share Capital A/c (470 × ₹10)	Dr.		4,700	
	Securities Premium A/c (470 × ₹5)	Dr.		2,350	
	To Calls in Arrears A/c (470 × ₹13)				6,110
	To Forfeited Shares A/c (470 × ₹2)				940
	(470 shares forfeited due to non payment of allotment and call money)				
	Bank A/c (60 × ₹14)	Dr.		840	
	To Equity Share Capital A/c (60 × ₹10)				600
	To Securities Premium Reserve A/c (60 × ₹4)				240
	(60 shares re-issued @₹14 per share)				
	Forfeited Shares(1)	Dr.		120	
	To Capital Reserve A/c				120
	(Gain on re-issue transferred to Capital Reserve A/c)				

Dr. FORFEITED SHARES ACCOUNT Cr.

Particulars	₹	*Particulars*	₹
To Capital Reserve A/c	120	By Equity Share Capital A/c	940
To Balance c/d	820		
	940		940

Working Note (1) Forfeited amount on 470 Shares = ₹940

∴ Forfeited amount on 60 Shares = $₹940 \times \frac{60}{470} = ₹120$

ILLUSTRATION 40.

Give Journal entries for forfeiture and reissue of shares :

(*a*) Carbon Ltd. forfeited 800 shares of ₹20 each issued at a premium of ₹2 per share (₹18 called up) on which first call of ₹4 per share was not paid.

Of these, 300 shares were re-issued @ ₹15 per share as ₹18 paid up.

(ISC Sample Paper, 2017)

(*b*) *X* Ltd. forfeited 1,000 shares of ₹10 each issued at 10% premium to Shyam (₹9 called up) on which he did not pay ₹3 of allotment (including premium) and first call of ₹2. Out of these, 600 shares were re-issued to Ram as fully paid up for ₹8 per share and 200 shares to Dham as fully paid up @ ₹12 at different intervals of time.

SOLUTION : (a)

Date	*Particulars*		*L.F.*	*Dr.*	*Cr.*
				₹	₹
	Share Capital A/c	Dr.		14,400	
	To Calls in Arrears A/c				3,200
	To Share Forfeiture A/c				11,200
	(Forfeiture of 800 shares)				
	Bank A/c	Dr.		4,500	
	Share Forfeiture A/c	Dr.		900	
	To Share Capital A/c				5,400
	(Re-issue of 300 shares @ ₹15 per share, as ₹18 paid up)				
	Share Forfeiture A/c(1)	Dr.		3,300	
	To Capital Reserve A/c				3,300
	(Gain on 300 re-issued shares transferred to Capital Reserve)				

Note : (1)

		₹
Forfeited amount on 800 shares	= ₹11,200	
Forfeited amount on 300 shares	$= ₹11{,}200 \times \frac{300}{800} =$	4,200
Less : Loss on Re-issue of 300 shares @ ₹3 each		900
Transferred to Capital Reserve		3,300

(b)

Date	*Particulars*		*L.F.*	*Dr.*	*Cr.*
				₹	₹
	Share Capital A/c	Dr.		9,000	
	Securities Premium Reserve A/c	Dr.		1,000	
	To Calls in Arrears A/c				5,000
	To Share Forfeiture A/c				5,000
	(Forfeiture of 1,000 shares of Shyam)				
	Bank A/c	Dr.		4,800	
	Share Forfeiture A/c	Dr.		1,200	
	To Share Capital A/c				6,000
	(Re-issue of 600 shares at ₹8 per share as fully paid up)				
	Share Forfeiture A/c(2)	Dr.		1,800	
	To Capital Reserve A/c				1,800
	(Gain on 600 shares transferred to capital reserve)				
	Bank A/c	Dr.		2,400	
	To Share Capital A/c				2,000
	To Securities Premium Reserve A/c				400
	(200 shares re-issued, after sometime)				
	Share Forfeiture A/c(3)	Dr.		1,000	
	To Capital Reserve A/c				1,000
	(Gain on 200 shares transferred)				

600 shares and 200 shares have been re-issued at different intervals of time. Therefore, entry for their re-issue have been made separately.

				₹
Note : (2) Forfeited amount on 1,000 shares	=	₹5,000		
Forfeited amount on 600 shares	=	₹5,000 × $\frac{600}{1,000}$	=	3,000
Less : Loss on Re-issue				1,200
Transferred to Capital Reserve :				1,800

Note : (3) Forfeited amount on 1,000 shares	=	₹5,000		
Forfeited amount on 200 shares	=	₹5,000 × $\frac{200}{1,000}$	=	1,000

ILLUSTRATION 41.

Rupa Ltd. issued 5,00,000 equity shares of ₹10 each at a premium of ₹15 per share. The amounts were receivable as follows :

	Capital	*Premium*	*Total*
	₹	₹	₹
On Application	2	6	8
On Allotment	3	5	8
On Final Call	5	4	9
	10	15	25

All amounts were received except final call on 500 shares held by Mr. Dushyant. His shares were forfeited and were reissued to Mr. Bharat at a price of ₹14 per share.

You are asked to pass the Journal entries on forfeiture and re-issue.

Books of Rupa Ltd.

Date	*Particulars*			*L.F.*	*Dr.*	*Cr.*
					₹	₹
	Equity Share Capital A/c	500 × ₹10	Dr.		5,000	
	Securities Premium Reserve A/c	500 × ₹ 4	Dr.		2,000	
	To Calls in Arrears A/c	500 × ₹ 9				4,500
	To Forfeited Shares A/c	500 × ₹ (2 + 3)				2,500
	(Forfeiture of 500 Shares for non-payment of final call)					
	Bank A/c		Dr.		7,000	
	To Equity Share Capital A/c					5,000
	To Securities Premium Reserve A/c					2,000
	(Reissue of forfeited shares as fully paid up at ₹14 per share)					
	Forfeited Shares A/c		Dr.		2,500	
	To Capital Reserve A/c					2,500
	(Gain on reissue of forfeited shares transferred to Capital Reserve)					

CASE BASED MCQs — 2

India Ltd. invited applications for issuing 3,00,000 equity shares of ₹10 each at a premium of ₹30 per share. The amount was payable as follows :

On Applications	: ₹7 per share	(including ₹5 premium)
On Allotment	: ₹10 per share	(including ₹7 premium)
On First Call	: ₹11 per share	(including ₹8 premium)
On Second and Final Call	: Balance Amount	

A shareholder holding 2,000 shares did not pay the first call and second and final call money and his shares were forfeited after the final call.

(*a*) Share Forfeiture Account will be Credited by :

(*i*) ₹34,000
(*ii*) ₹10,000
(*iii*) ₹24,000
(*iv*) ₹14,000

(*b*) Securities Premium Reserve Account will be debited by :

(*i*) ₹36,000
(*ii*) ₹60,000
(*iii*) ₹24,000
(*iv*) ₹20,000

(*c*) Calls in Arrears Account will be credited by :

(*i*) ₹10,000
(*ii*) ₹24,000
(*iii*) ₹22,000
(*iv*) ₹46,000

(*d*) Liability of a shareholder is limited to .... of the shares allotted to him.

(*i*) Face Value
(*ii*) Called up value
(*iii*) Paid up value
(*iv*) Uncalled up value

CASE BASED MCQs — 3

X Ltd. issued a prospectus inviting applications for 5,00,000 shares of ₹10 each at a premium of ₹14 per share, payable as follows :

On Application	₹8 (including ₹5 premium)
On Allotment	₹7 (including ₹4 premium)
On First Call	₹5 (including ₹3 premium)
On Second & Final Call	Balance Amount

A shareholder holding 800 shares failed to pay the allotment money and his shares were forfeited after allotment.

(*a*) In the entry for forfeiture of shares, Share Capital Account will be debited with :

(*i*) ₹2,400
(*ii*) ₹5,600
(*iii*) ₹4,800
(*iv*) ₹8,000

(*b*) Securities Premium Reserve A/c will be debited by :

(*i*) ₹7,200
(*ii*) ₹ 4,000
(*iii*) ₹3,200
(*iv*) ₹11,200

(*c*) Share Forfeiture A/c will be credited by :

(*i*) ₹6,400
(*ii*) ₹4,800
(*iii*) ₹4,000
(*iv*) ₹2,400

(*d*) Which of the following is *not* a Capital profit :

(*i*) Profit on Forfeiture and reissue of shares

(*ii*) Profit earned by a Company after its incorporation
(*iii*) Securities Premium on issue of shares
(*iv*) Profit on sale of fixed assets

CASE BASED MCQs — 4

Johri Ltd. was formed with an authorised capital of ₹10,00,000 divided into shares of ₹20 each. It offered 40,000 shares to the public for subscription at a premium of ₹10 per share. Applications were received for 37,000 shares and allotment was made to all applicants. Amounts were payable as follows :

On Application	₹6
On Allotment	₹15 (including premium)
On Ist Call	₹5
On IInd & Final Call	Balance

It forfeited 3,000 shares of ₹20 each (₹16 called up) held by Mansi, for non-payment of allotment and the first call. Out of these, 2,000 shares were reissued to Sudha as ₹16 called up for ₹14 per share.

(*a*) Amount transferred to capital reserve will be :

(*i*) ₹14,000 (*ii*) ₹18,000
(*iii*) NIL (*iv*) ₹ 8,000

(*b*) Balance of Share Forfeiture Account will be :

(*i*) ₹14,000 (*ii*) ₹18,000
(*iii*) ₹ 6,000 (*iv*) ₹10,000

(*c*) Subscribed and Fully Paid Capital will be :

(*i*) ₹5,76,000 (*ii*) NIL
(*iii*) ₹5,82,000 (*iv*) ₹7,40,000

(*d*) Subscribed but not Fully Paid Capital will be :

(*i*) ₹5,76,000 (*ii*) ₹5,82,000
(*iii*) ₹7,20,000 (*iv*) ₹7,26,000

(*e*) Securities Premium Reserve cannot be utilized for :

(*i*) Buy-back of its own shares
(*ii*) Issuing partly paid bonus shares to shareholders
(*iii*) Issuing fully paid bonus shares to shareholders
(*iv*) Writing off preliminary expenses of the Company

CASE BASED MCQs — 5

Z Ltd. invited applications for issuing 3,00,000 equity shares of ₹20 each at a premium of ₹30 per share. The amount was payable as follows :

On Application	₹10 per share (including ₹6 premium)
On Allotment	₹13 per share (including ₹7 premium)
On First Call	₹13 per share (including ₹8 premium)
On Second and Final Call	Balance Amount

Vishakha, a shareholder holding 500 shares, did not pay the allotment and first call money and her shares were forfeited after first call.

(*a*) Calls in Arrears Account will be Credited by :

(*i*) ₹ 5,500
(*ii*) ₹20,000
(*iii*) ₹13,000
(*iv*) ₹ 8,000

(*b*) Securities Premium Reserve A/c will be debited by :

(*i*) ₹10,500
(*ii*) ₹ 7,500
(*iii*) ₹12,000
(*iv*) ₹15,000

(*c*) Share Forfeiture A/c will be credited by :

(*i*) ₹5,000
(*ii*) ₹3,000
(*iii*) ₹8,000
(*iv*) ₹2,000

(*d*) Share Capital Account will be debited by

(*i*) ₹5,500
(*ii*) ₹10,000
(*iii*) ₹7,500
(*iv*) ₹13,000

CASE BASED MCQs — 6

Xylo Ltd. was formed on 1st April, 2018, with an authorized capital of ₹12,00,000 divided into equity shares of ₹10 each.

It invited applications for 30,000 shares to be issued at par, in the year of its formation, all of which were subscribed for and the amount due on them fully received.

On 1st April, 2020, the company issued another 60,000 shares at a premium of ₹2 per share to be received with allotment. It received applications for 55,000 shares which were duly allotted.

All amounts due on the allotted shares was received except the final call of ₹2 per share on 1,000 shares. The company forfeited these shares and later reissued 800 of the forfeited shares @ ₹7 per share fully called up.

The Balance Sheet of the company was prepared as at 31st March, 2021, as per Schedule III of the Companies Act, 2013.

(*a*) The issued capital of the company to be shown in Notes to Accounts as at 31st March, 2021, under "Share Capital" will be:

(*i*) ₹12,00,000
(*ii*) ₹9,00,000
(*iii*) ₹ 8,50,000
(*iv*) ₹8,49,600

(*b*) The subscribed shares of the company at the end of the year 2020-21 will be:

(*i*) ₹1,20,000
(*ii*) ₹90,000
(*iii*) ₹ 85,000
(*iv*) ₹84,800

(*c*) The amount of Share Capital to be shown in the Balance Sheet of the company as at 31st March, 2021, will be:

(*i*) ₹12,00,000
(*ii*) ₹9,00,000
(*iii*) ₹ 8,50,000
(*iv*) ₹8,49,600

(*d*) The net gain made by the company on reissue of the 800 shares will be transferred to:

(*i*) Reserve Capital Account
(*ii*) Capital Reserve Account
(*iii*) Securities Premium Reserve Account
(*iv*) Statement of P/L

(I.S.C. Sample Paper, 2021)

CASE BASED MCQs — 7

Happy Days Ltd. was formed with an authorised capital of ₹50,00,000 divided into 5,00,000 equity shares of ₹10 each. The company issued prospectus inviting applications for 4,00,000 equity shares. The company received applications for 3,70,000 equity shares. During the first year, ₹8 per share were called. Suman holding 7,000 shares and Zia holding 5,000 shares did not pay the first call of ₹3 per share. Zia's shares were forfeited after the first call and later on 3,000 of the forfeited shares were re-issued at ₹7 per share, ₹8 called up.

(*a*) Calls in Arrears will be :

(*i*) ₹15,000 (*ii*) ₹21,000
(*iii*) Nil (*iv*) ₹36,000

(*b*) Subscribed and Fully Paid Capital will be :

(*i*) ₹36,80,000 (*ii*) ₹36,69,000
(*iii*) ₹29,13,000 (*iv*) Nil

(*c*) Subscribed but not Fully Paid Capital will be :

(*i*) ₹29,44,000 (*ii*) ₹29,33,000
(*iii*) ₹29,23,000 (*iv*) ₹36,69,000

(*d*) In the Balance Sheet of a company, under the heading share capital, at the last is shown :

(*i*) Authorised Share Capital (*ii*) Subscribed Share Capital
(*iii*) Issued Share Capital (*iv*) Reserve Share Capital

(*e*) For what purpose securities premium reserve account cannot be utilized?

(*i*) Amortization of preliminary expenses
(*ii*) Issue of Fully Paid Bonus Shares
(*iii*) Distribution of Dividend
(*iv*) Buy Back of own shares

(See Answers at the end of the book)

Forfeiture in Case of Over-subscription and Pro-rata Allotment

ILLUSTRATION 42.

Nav Lakshmi Ltd. issued a prospectus inviting applications for 50,000 shares of ₹10 each. These shares were issued at par on the following terms :

On application ₹3, on allotment ₹4, on first call ₹2 and on final call the balance.

Applications were received for 60,000 shares. Allotments were made on the following basis :

(*i*) To applicants for 10,000 shares — in full;
(*ii*) To applicants for 20,000 shares — 15,000 shares;
(*iii*) To applicants for 30,000 shares — 25,000 shares.

All excess amount paid on application is to be adjusted against amount due on allotment.

The shares were fully called and paid up except the amount of allotment, first and final call not paid by those who applied for 2,000 shares of the group applying for 20,000 shares.

All the shares on which calls were not paid were forfeited by the Board of Directors.

1,000 forfeited shares were re-issued as fully paid on receipt of ₹8 per share.

Show the journal entries in the books of Nav Lakshmi Ltd.

SOLUTION: JOURNAL

Date	Particulars		L.F.	Dr.	Cr.
				₹	₹
	Bank A/c	Dr.		1,80,000	
	To Share Application A/c				1,80,000
	(Application money received on 60,000 shares @ ₹3 per share)				
	Share Application A/c	Dr.		1,80,000	
	To Share Capital A/c				1,50,000
	To Share Allotment A/c				30,000
	(Application money transferred to share capital account and the excess money to share allotment account)				
	Share Allotment A/c	Dr.		2,00,000	
	To Share Capital A/c				2,00,000
	(Allotment money due on 50,000 shares @ ₹4 per share)				
	Bank A/c(1)	Dr.		1,65,500	
	Calls in Arrears A/c	Dr.		4,500	
	To Share Allotment A/c				1,70,000
	(Allotment money received, except on 1,500 shares)				
	Share First Call A/c	Dr.		1,00,000	
	To Share Capital A/c				1,00,000
	(First call due on 50,000 shares @ ₹2 per share)				
	Bank A/c	Dr.		97,000	
	Calls in Arrears A/c	Dr.		3,000	
	To Share First Call A/c				1,00,000
	(First call money received, except on 1,500 shares @ ₹2 per share)				
	Share Final Call A/c	Dr.		50,000	
	To Share Capital A/c				50,000
	(Final call due on 50,000 shares @ ₹1 per share)				
	Bank A/c	Dr.		48,500	
	Calls in Arrears A/c	Dr.		1,500	
	To Share Final Call A/c				50,000
	(Final call received, except on 1,500 shares @ ₹1 per share)				
	Share Capital A/c	Dr.		15,000	
	To Calls in Arrears A/c				9,000
	To Share Forfeiture A/c				6,000
	(Forfeiture of 1,500 shares)				

	Bank A/c Dr. Share Forfeiture A/c Dr. To Share Capital A/c (Re-issue of 1,000 shares at ₹8 per share)		8,000 2,000	10,000
	Share Forfeiture A/c(2) Dr. To Capital Reserve A/c (Gain on 1,000 forfeited shares transferred to Capital Reserve A/c)		2,000	2,000

Working Notes :

(1) (A) As Applicants for 20,000 shares were allotted = 15,000 shares

∴ Applicants for 2,000 shares were allotted $= \frac{15,000}{20,000} \times 2,000 = 1,500$ shares

Excess application money received on these :

(2,000 shares – 1,500 shares) × ₹3 = ₹1,500

(B) Amount due on allotment on these shares =1,500 shares × ₹4 = ₹6,000

Less : Excess received on application from these shares = ₹1,500

Amount not received on allotment = ₹4,500

(C) Amount received on allotment :

	₹
Total amount due on allotment 50,000 shares × ₹4	= 2,00,000
Less : Excess amount received on applications 10,000 Shares × ₹3	= 30,000
Balance Due	= 1,70,000
Less : Amount not received on allotment	= 4,500
Net Amount received on allotment in Cash	= 1,65,500

(2) Since only 1,000 shares have been re-issued, therefore the profit on 1,000 shares will be transferred to Capital Reserve.

Forfeited amount on 1,500 shares = ₹6,000

	₹
∴ Forfeited amount on 1,000 shares= ₹ $\frac{6,000}{1,500} \times 1,000$ =	4,000
Less : Loss on re-issue of 1,000 shares @ ₹2 per share =	2,000
Amount transferred to Capital Reserve =	2,000

ILLUSTRATION 43.

AB Ltd. invited applications for 1,00,000 Equity Shares of ₹10 each, payable as ₹2 on application, ₹3 on allotment and the balance on first and final call. Applications were received for 3,00,000 shares and the shares were allotted on a pro rata basis. The excess application money was to be adjusted against allotment only. *M*, a shareholder, who had applied for 3,000 shares, failed to pay the call money and his shares were accordingly forfeited and reissued at ₹8 per share as fully paid.

SOLUTION : JOURNAL

Date	*Particulars*	*L.F.*	*Dr.* (₹)	*Cr.* (₹)
	Bank A/c Dr. To Equity Share Application A/c (Application money received on 3,00,000 shares @ ₹2 per share)		6,00,000	6,00,000

Equity Share Application A/c	Dr.	6,00,000	
To Equity Share Capital A/c (1,00,000 × ₹2)			2,00,000
To Equity Share Allotment A/c (1,00,000 × ₹3)			3,00,000
To Bank A/c			1,00,000
(Application money adjusted to Share Capital A/c and Share Allotment A/c and balance refunded to applicants)			
Equity Share Allotment A/c	Dr.	3,00,000	
To Equity Share Capital A/c			3,00,000
(Allotment due on 1,00,000 shares @ ₹3 per share)			
Equity Share First & Final Call A/c	Dr.	5,00,000	
To Equity Share Capital A/c			5,00,000
(First & Final Call due on 1,00,000 shares @ ₹5 per share)			
Bank A/c	Dr.	4,95,000	
Calls in Arrears A/c	Dr.	5,000	
To Equity Share First & Final Call A/c			5,00,000
(Call money received, except on 1,000 shares @ ₹5 per share)			
Equity Share Capital A/c	Dr.	10,000	
To Calls in Arrears A/c			5,000
To Share Forfeiture A/c			5,000
(Forfeiture of 1,000 shares)			
Bank A/c	Dr.	8,000	
Share Forfeiture A/c	Dr.	2,000	
To Equity Share Capital A/c			10,000
(Reissue of 1,000 shares @ ₹8 per share)			
Share Forfeiture A/c	Dr.	3,000	
To Capital Reserve A/c			3,000
(Transfer of gain on reissue)			

Working Notes :

(*i*) Applicants for 3,00,000 shares have been allotted 1,00,000 shares
Hence, *M* who had applied for 3,000 shares must have been allotted

$$= \frac{1{,}00{,}000}{3{,}00{,}000} \times 3{,}000 = 1{,}000 \text{ shares}$$

(*ii*) Since all amount due on allotment has already been received on application, there would be no entry for receipt of allotment money.

Over-subscription and Forfeiture of Shares Issued at a Premium :

In such type of questions, a problem arises whether Securities Premium Reserve Account should be debited or not at the time of forfeiture. In order to solve the problem, it will have to be observed that if the premium is due on allotment, then, whether the excess application money received on forfeited shares has been utilised to meet the amount of share capital due on allotment or it has been utilised to meet the premium due on allotment.

In this edition of the book, the excess application money has been utilised for the share capital due on allotment. Hence, in such type of questions where the premium is due on allotment and where the shares are forfeited for non-payment of allotment money, 'Securities Premium Reserve Account' has been debited in entry for forfeiture.

ILLUSTRATION 44.

The Delhi Cloth Mills Ltd. invited applications for 10,000 Shares of ₹100 each at a premium of ₹10 each payable as below :

₹50 on Application;
₹35 on Allotment (including premium), and
₹25 on Call.

Applications for 15,000 shares were received. Applicants for 2,500 shares did not get any allotment and their money returned. Allotment was made *pro-rata* to the remaining applicants.

Mr. *A* was allotted 400 shares. He failed to pay the amount due on allotment and call money. The company forfeited his shares and subsequently re-issued at ₹105 per share.

Show the journal entries in the books of the company and also prepare the Balance Sheet.

SOLUTION :

JOURNAL

Date	*Particulars*		*L.F.*	*Dr.*	*Cr.*
				₹	₹
	Bank A/c	Dr.		7,50,000	
	To Share Application A/c				7,50,000
	(Amount received on application)				
	Share Application A/c	Dr.		7,50,000	
	To Share Capital A/c				5,00,000
	To Share Allotment A/c				1,25,000
	To Bank A/c (2,500 × ₹50)				1,25,000
	(Application money adjusted)				
	Share Allotment A/c	Dr.		3,50,000	
	To Share Capital A/c				2,50,000
	To Securities Premium Reserve A/c				1,00,000
	(Allotment money, including premium due on 10,000 shares at ₹35 per share)				
	Bank A/c[4]	Dr.		2,16,000	
	Calls in Arrears A/c	Dr.		9,000	
	To Share Allotment A/c				2,25,000
	(Amount received on allotment except on 400 shares of *A*)				
	Share First and Final Call A/c	Dr.		2,50,000	
	To Share Capital A/c				2,50,000
	(First and final call due on 10,000 shares at ₹25 per share)				

Bank A/c	Dr.	2,40,000	
Calls in Arrears A/c	Dr.	10,000	
To Shares First and Final Call A/c			2,50,000
(First call received on 9,600 shares @ ₹25 per share)			
Share Capital A/c	Dr.	40,000	
Securities Premium Reserve A/c	Dr.	4,000	
To Calls in Arrears A/c			19,000
To Share Forfeiture A/c			25,000
(Forfeiture of 400 shares of *A*)			
Bank A/c	Dr.	42,000	
To Share Capital A/c			40,000
To Securities Premium Reserve A/c			2,000
(Reissue of 400 forfeited shares @ ₹105 per share)			
Share Forfeiture A/c	Dr.	25,000	
To Capital Reserve A/c			25,000
(Balance of Share Forfeiture A/c transferred to Capital Reserve A/c)			

BALANCE SHEET OF DELHI CLOTH MILLS LTD. *as at* ....

Particulars	*Note No.*	*Current year*	*Previous year*
I. EQUITY AND LIABILITIES :		₹	₹
Shareholder's Funds :			
(*a*) Share Capital	1	10,00,000	
(*b*) Reserve and Surplus	2	1,23,000	
		11,23,000	
II. ASSETS :			
Current Assets :			
Cash and Bank Balance	3	11,23,000	

Notes to Accounts :

	₹	₹
(1) Share Capital :		
Authorised Share Capital :		
.... Shares of ₹100 each	....	
Issued Subscribed and Fully Paid Capital :		
10,000 Shares of ₹100 each	10,00,000	
(2) Reserve and Surplus :		
Securities Premium Reserve A/c	98,000	
Capital Reserve A/c	25,000	
	1,23,000	
(3) Cash and Bank Balance :		
Cash at Bank	11,23,000	

(ii) (A) Excess amount received from *A* on application :

A has been allotted 400 shares. He must have applied for more shares.

If shares allotted were 10,000, shares applied for were = 12,500

$\therefore$ If shares allotted were 400, shares applied for were $= \dfrac{12{,}500}{10{,}000} \times 400 = 500$ shares

Excess application money received from *A* :

500 Shares – 400 Shares = 100 Shares × ₹50 = ₹5,000

		₹
(B) Amount due from *A* on allotment :		
400 Shares × ₹35	=	14,000
Less : Excess received from *A* on application	=	5,000
Net amount due from *A* on allotment, which has not been received	=	9,000
(C) Total amount due on Allotment 10,000 Shares × ₹35	=	3,50,000
Less : Excess amount received on applications	=	1,25,000
Balance Due	=	2,25,000
Less : Amount not received from *A* on allotment	=	9,000
Net amount received on allotment in Cash	=	2,16,000

ILLUSTRATION [illegible]

X Ltd. issued for Public subscription 40,000 equity shares of ₹10 each at a premium of ₹2 per share payable as under; on application ₹4 per share; on allotment ₹5 per share (including premium and on call ₹3 per share.

Applications were received for 60,000 shares. Allotment was made *pro-rata* to the applicants for 48,000 shares, the remaining applications being refused. Money overpaid on application was utilised towards sums due on allotment.

Shri Manoj, to whom 1,500 shares were allotted, failed to pay the allotment and call money and Shri Hussain to whom 2,000 shares were allotted failed to pay the call money. These shares were subsequently forfeited. All the forfeited shares were sold to Shri Banerjee as fully paid up at ₹8 per share. Show the journal entries to record the above transactions and prepare the Balance Sheet.

SOLUTION :

JOURNAL OF *X* LTD.

Date	*Particulars*		*L.F.*	*Dr.*	*Cr.*
				₹	₹
	Bank A/c	Dr.		2,40,000	
	To Equity Share Application A/c				2,40,000
	(Application money received on 60,000 shares @ ₹4 per share)				
	Equity Share Application A/c	Dr.		2,40,000	
	To Equity Share Capital A/c				1,60,000
	To Equity Share Allotment A/c				32,000
	To Bank A/c				48,000
	(Application money transferred to Share Capital A/c for 40,000 shares; to Allotment A/c for 8,000 shares and amount returned on 12,000 shares @ ₹4 per				

	Equity Share Allotment A/c	Dr.		2,00,000	
	To Equity Share Capital A/c				1,20,000
	To Securities Premium Reserve A/c				80,000
	(Allotment due on 40,000 shares @ ₹5 per share)				
	Bank A/c[4]	Dr.		1,61,700	
	Calls in Arrears A/c	Dr.		6,300	
	To Equity Share Allotment A/c				1,68,000
	(Allotment money received except on 1,600 shares of Manoj)				
	Equity Share First and Final Call A/c	Dr.		1,20,000	
	To Equity Share Capital A/c				1,20,000
	(Final call due on 40,000 shares @ ₹3 per share)				
	Bank A/c	Dr.		1,09,500	
	Calls in Arrears A/c	Dr.		10,500	
	To Equity Share First and Final Call A/c				1,20,000
	(Final call received except on 3,500 shares @ ₹3 per share)				
	Equity Share Capital A/c	Dr.		35,000	
	Securities Premium Reserve A/c[5]	Dr.		3,000	
	To Calls in Arrears A/c				16,800
	To Share Forfeiture A/c				21,200
	(Forfeiture of 3,500 shares)				
	Bank A/c	Dr.		28,000	
	Share Forfeiture A/c	Dr.		7,000	
	To Equity Share Capital A/c				35,000
	(Re-issue of 3,500 shares at ₹8 per share)				
	Share Forfeiture A/c	Dr.		14,200	
	To Capital Reserve A/c				14,200
	(Balance of Share Forfeiture A/c transferred to Capital Reserve A/c)				

BALANCE SHEET OF *X* LTD.

as at ....

Particulars	*Note No.*	*Current year*	*Previous year*
I. EQUITY AND LIABILITIES :		₹	₹
Shareholder's Funds :			
(*a*) Share Capital	1	4,00,000	
(*b*) Reserve and Surplus	2	91,200	
		4,91,200	
II. ASSETS :			
Current Assets :			
Cash and Bank Balance	3	4,91,200	

Notes to Accounts :

	₹	₹
(1) **Share Capital :**		
Authorised Capital :		
.... Shares of ₹ .... each	....	
Issued, Subscribed and Fully Paid Capital :		
40,000 Equity Shares of ₹10 each	4,00,000	
(2) **Reserves and Surplus :**		
Capital Reserve	14,200	
Securities Premium Reserve A/c	77,000	
	91,200	
(3) **Cash and Bank Balance :**		
Cash at Bank	4,91,200	

(4) (A) Excess amount received from Manoj on application :

Manoj has been allotted 1,500 shares. He must have applied for more shares.

If shares allotted were 40,000, shares applied for were = 48,000

∴ If shares allotted were 1,500 shares applied for were $= \frac{48,000}{40,000} \times 1,500 = 1,800$ shares.

Excess application money received from Manoj = 1,800 shares – 1,500 shares
= 300 shares × ₹4 = ₹1,200

(B) Amount due from Manoj on allotment :

1,500 shares × ₹5 = ₹7,500

Less : Excess received from Manoj on application = ₹1,200

Net amount due from Manoj on allotment, which has not been received = ₹6,300

		₹
(C) Total amount due on allotment 40,000 shares × ₹5	=	2,00,000
Less : Excess amount received on applications	=	32,000
Balance Due	=	1,68,000
Less : Amount not received from Manoj on allotment	=	6,300
Net amount received on allotment in cash	=	1,61,700

(5) Premium is due with allotment and only Manoj has not paid the amount of allotment. Therefore, Securities Premium Reserve Account has been debited from the amount of premium due from Manoj only *i.e.*, 1,500 shares × ₹2 = ₹3,000.

ILLUSTRATION 46.

A limited company issued a prospectus inviting applications for 2,00,000 shares of ₹10 each at a premium of ₹2 per share payable as follows: On Application ₹3; On Allotment ₹4 (including premium) : On First Call ₹3 and On Second Call ₹2.

Applications were received for 3,00,000 shares and allotment was made on *pro-rata* basis. Money overpaid on applications was employed on account of sums due on allotment.

R, to whom 400 shares were allotted failed to pay the allotment money and on his subsequent failure to pay the First Call his shares were forfeited. *M*, the holder of 600 shares failed to pay the two calls and his shares were forfeited after the Second Call. Of the shares forfeited, 800 shares were sold to *K* as fully paid, *K* paying ₹9 per share, the whole of *R*'s share being included.

Give journal entries, prepare Bank Account and Balance Sheet.

SOLUTION:

JOURNAL

Date	*Particulars*	*L.F.*	*Dr.* ₹	*Cr.* ₹
	Bank A/c Dr. To Share Application A/c (Application money received on 3,00,000 shares @ 3 per share)		9,00,000	 9,00,000
	Share Application A/c Dr. To Share Capital A/c To Share Allotment A/c (Application money transferred to Share Capital A/c for 2,00,000 shares @ ₹3 per share and to Allotment A/c for 1,00,000 shares @ ₹3 per share.)		9,00,000	 6,00,000 3,00,000
	Share Allotment A/c Dr. To Share Capital A/c To Securities Premium Reserve A/c (Allotment due on 2,00,000 shares @ ₹4 per share)		8,00,000	 4,00,000 4,00,000
	Bank A/c$^{(4)}$ Dr. Calls in Arrears A/c Dr. To Share Allotment A/c (Allotment money received except on 400 shares of *R*)		4,99,000 1,000	 5,00,000
	Share First Call A/c Dr. To Share Capital A/c (First call due on 2,00,000 shares at ₹3 per share)		6,00,000	 6,00,000
	Bank A/c Dr. Calls in Arrears A/c Dr. To Share First Call A/c (First call money received, except on 400 shares of *R* and 600 shares of *M*)		5,97,000 3,000	 6,00,000
	Share Capital A/c Dr. Securities Premium Reserve A/c$^{(5)}$ Dr. To Calls in Arrears A/c To Share Forfeiture A/c (Forfeiture of 400 shares of *R*; Share Capital A/c debited @ ₹8 per share called up)		3,200 800	 2,200 1,800
	Share Second Call A/c Dr. To Share Capital A/c (Second call money due on 1,99,600 shares at ₹2 per share)		3,99,200	 3,99,200

	Bank A/c	Dr.		3,98,000	
	Calls in Arrears A/c	Dr.		1,200	
	To Share Second Call A/c				3,99,200
	(Second call money received on 1,99,000 shares)				
	Share Capital A/c(6)	Dr.		6,000	
	To Calls in Arrears A/c				3,000
	To Share Forfeiture A/c				3,000
	(Forfeiture of 600 shares of *M*)				
	Bank A/c	Dr.		7,200	
	Share Forfeiture A/c	Dr.		800	
	To Share Capital A/c				8,000
	(800 shares re-issued at ₹9 per share)				
	Share Forfeiture A/c(7)	Dr.		3,000	
	To Capital Reserve A/c				3,000
	(Gain on 800 re-issued shares transferred to Capital Reserve A/c)				

Dr. BANK ACCOUNT Cr.

Particulars	₹	*Particulars*	₹
To Share Application A/c	9,00,000	By Balance c/d	24,01,200
To Share Allotment A/c(3)	4,99,000		
To Share First Call A/c	5,97,000		
To Share Second Call A/c	3,98,000		
To Share Capital A/c	7,200		
	24,01,200		24,01,200

Note : In the above question a Cash Book is not required. However, if a Cash Book is asked, the Bank A/c as prepared above will become a Cash Book and Cash transactions will not be recorded in journal.

BALANCE SHEET

as at ....

Particulars	*Note No.*	*Current year*	*Previous year*
I. EQUITY AND LIABILITIES :		₹	₹
Shareholder's Funds :			
(*a*) Share Capital	1	19,99,000	
(*b*) Reserve and Surplus	2	4,02,200	
		24,01,200	
II. ASSETS :			
Current Assets :			
Cash and Bank Balance	3	24,01,200	

Notes to Accounts :

		₹	₹
(1) **Share Capital :**			
Authorised :			
.... Shares of ₹ .... each		....	
Issued :			
2,00,000 shares of ₹10 each fully paid		20,00,000	
Subscribed and Fully Paid Capital :			
1,99,800 Shares of ₹10 each	19,98,000		
Add : Share Forfeiture A/c	1,000(8)	19,99,000	
(2) **Reserve and Surplus**			
Capital Reserve A/c		3,000	
Securities Premium Reserve A/c		3,99,200	
		4,02,200	
(3) **Cash and Bank Balance :**			
Cash at Bank		24,01,200	

(4) (A) Excess amount received from *R* on application :

R has been allotted 400 shares. He must have applied for more shares.

If shares allotted were 2,00,000, shares applied for were = 3,00,000

∴ If shares allotted were 400, shares applied for were $= \frac{3,00,000}{2,00,000} \times 400$

= 600 shares.

Excess application money received from *R* = 600 shares – 400 shares

= 200 shares × ₹3 = ₹600

		₹
(B) Amount due from *R* on allotment : 400 shares × ₹4	=	1,600
Less : Excess received from *R* on application	=	600
Net amount due from *R* on allotment, which has not been received		1,000

(C) Total amount due on allotment 2,00,000 shares × ₹4	=	8,00,000
Less : Excess amount received on application (1,00,000 shares × ₹3)	=	3,00,000
Balance Due	=	5,00,000
Less : Amount not received from *R* on allotment	=	1,000
Net amount received on allotment	=	4,99,000

(5) Premium is due with allotment. *R* has not paid the amount of allotment. Therefore, Securities Premium Reserve A/c will be debited by 400 shares × ₹2 = ₹800.

(6) *M* has paid the amount of allotment. Therefore, he has paid premium also. Premium once collected cannot be cancelled. As such 'Securities Premium Reserve A/c' will not be debited when his shares are forfeited.

(7) Only 800 shares are re-issued. Therefore, the gain on 800 shares will only be transferred to Capital Reserve :

		₹
Forfeited amount on 400 shares of *R*	=	1,800
Forfeited amount on 400 shares of $M = \frac{₹3,000}{600 \text{ shares}} \times 400$ shares	=	2,000
		3,800
Less : Loss on re-issue of 800 shares @ ₹1 each		800
		3,000

(8) Forfeited amount on 600 shares of *M* was ₹3,000, out of which 400 shares have been re-issued. Therefore, the balance of forfeited amount remaining in Share Forfeiture A/c for 200 shares $= \frac{3,000}{600} \times 200 =$ ₹1,000. This balance of ₹1,000 will be shown on the equity & liabilities side of the Balance Sheet under the head 'Share Capital'.

ILLUSTRATION 47.

Reliable Ltd. was registered with an authorized capital of ₹20,00,000 in ₹10 per equity share. It invited applications for issuing 1,00,000 equity shares at a premium of ₹2 per share. The amount was payable as follows :

On application	₹4 per share (including premium)
On allotment	₹3 per share

Balance on 1st and Final Call.

Applications were received for 1,30,000 shares. Applications for 10,000 shares were rejected and the application money received on them was refunded. Pro-rata allotment was made to the remaining applications. Amount overpaid on these applications was adjusted towards the amount due on allotment. Sameer, who has applied for 1,200 shares, failed to pay the allotment and call money. The company forfeited his shares, out of which 800 shares were reissued to Sanjay at ₹9 per share fully paid up.

You are required to :

(*i*) Pass the Journal Entries in the books of the company through Calls in Arrears Account.

(*ii*) Prepare the Share Allotment Account. *(I.S.C. 2013)*

SOLUTION :

Reliable Ltd.

(*i*) JOURNAL

Date	*Particulars*		*L.F.*	*Dr.*	*Cr.*
				₹	₹
	Bank A/c	Dr.		5,20,000	
	To Share Application A/c				5,20,000
	(Application money received on 1,30,000 shares @ ₹4 per share)				

Share Application A/c	Dr.	5,20,000	
To Share Capital A/c			2,00,000
To Securities Premium Reserve A/c			2,00,000
To Share Allotment A/c			80,000
To Bank A/c			40,000
(Application money transferred to Share Capital @ ₹2 per share; Securities Premium @ ₹2 per share; to allotment account for 20,000 shares and application money refunded on 10,000 shares)			
Share Allotment A/c	Dr.	3,00,000	
To Share Capital A/c			3,00,000
(Allotment money due on 1,00,000 shares @ ₹3 per share)			
Bank A/c(1)	Dr.	2,17,800	
Calls-in-Arrears A/c	Dr.	2,200	
To Share Allotment A/c			2,20,000
(Allotment money received except on 1,000 shares)			
Share First and Final Call A/c	Dr.	5,00,000	
To Share Capital A/c			5,00,000
(First and final call made @ ₹5 per share)			
Bank A/c	Dr.	4,95,000	
Calls-in-Arrears A/c	Dr.	5,000	
To Share First and Final Call A/c			5,00,000
(Call money received except on 1,000 shares)			
Share Capital A/c (1,000 × ₹10)	Dr.	10,000	
To Forfeited Shares A/c			2,800
To Call-in-Arrears A/c			7,200
(Forfeiture of 1,000 shares of Sameer)			
Bank A/c (800 × ₹9)	Dr.	7,200	
Forfeited Shares A/c	Dr.	800	
To Share Capital A/c			8,000
(800 shares reissued @ ₹9 fully paid-up)			
Forfeited Shares A/c	Dr.	1,440	
To Capital Reserve A/c(2)			1,440
(Gain on 800 shares transferred to capital reserve)			

(*ii*) Dr. SHARE ALLOTMENT ACCOUNT Cr.

Particulars	₹	*Particulars*	₹
To Share Capital A/c	3,00,000	By Share Application A/c	80,000
		By Bank A/c	2,17,800
		By Calls in Arrears A/c	2,200
	3,00,000		3,00,000

1. (*a*) Shares Applied by Sameer = 1,200

Share Allotted to Sameer = $\frac{1,200 \times 1,00,000}{1,20,000}$ *i.e.*, 1,000 shares

Excess application money received from Sameer : 200 shares @ ₹4 = ₹800

(*b*) Amount due from Sameer on allotment :

	₹
1,000 shares @ ₹3 per share	3,000
Less : Excess received from Sameer on application	800
Net amount not received from Sameer on allotment	2,200

	₹
(*c*) Total amount due on allotment : 1,00,000 shares @ ₹3	3,00,000
Less : Excess amount received on application	80,000
	2,20,000
Less : Amount not received from Sameer	2,200
Net amount received on allotment in Cash	2,17,800

2. **Calculation of Amount transferred to Capital Reserve :**

	₹
Amount forfeited on 1,000 shares	2,800
∴ Amount forfeited on 800 shares (₹2,800 × 800/1,000)	2,240
Less : Discount allowed on 800 shares reissued	800
Gain on reissue transferred to Capital Reserve	1,440

ILLUSTRATION 48.

Saregama Ltd. invited applications for issuing 80,000 equity shares of ₹100 each at a premium of ₹10. The amount was payable as follows :

On Application — ₹30
On Allotment — ₹30 (including a premium of ₹10)
On 1st Call — ₹30
On Final Call — Balance

Applications for 1,20,000 shares were received. Allotment was made on pro rata basis to all applicants. Excess money received on application was adjusted on sums due on allotment. Dhwani, who was allotted 1,600 shares, failed to pay allotment money and Sargam who applied for 6,000 shares did not pay 1st call money. These shares were forfeited immediately after 1st Call.

2,000 of these shares (including all shares of Dhwani were reissued to Tarang for ₹95 per share as ₹80 paid up. Pass necessary journal entries in books of Saregama Ltd. by opening call in arrear account, if final call has not been made.

(C.B.S.E. Sample Paper, 2020)

SOLUTION : JOURNAL OF SAREGAMA LTD.

Date	*Particulars*		*L.F.*	*Dr.* (₹)	*Cr.* (₹)
	Bank A/c	Dr.		36,00,000	
	To Share Application A/c				36,00,000
	(Application money received)				
	Share Application A/c	Dr.		36,00,000	
	To Share Capital A/c				24,00,000
	To Share Allotment A/c				12,00,000
	(Application money transferred)				

	Share Allotment A/c Dr.		24,00,000	
	To Share Capital A/c			16,00,000
	To Security Premium Reserve A/c			8,00,000
	(Allotment money due)			
	Bank A/c[1] Dr.		11,76,000	
	Calls in Arrear A/c Dr.		24,000	
	To Share Allotment A/c			12,00,000
	(Allotment money received)			
	Share First Call A/c Dr.		24,00,000	
	To Share Capital A/c			24,00,000
	(First Call money due)			
	Bank A/c Dr.		22,32,000	
	Calls in Arrear A/c[2] Dr.		1,68,000	
	To Share First Call A/c			24,00,000
	(First Call money received)			
	Share Capital A/c (5,600 × ₹80) Dr.		4,48,000	
	Security Premium Reserve A/c (1,600 × ₹10) Dr.		16,000	
	To Calls in Arrear A/c			1,92,000
	To Share Forfeited A/c			2,72,000
	(5,600 shares forfeited)			
	Bank A/c Dr.		1,90,000	
	To Share Capital A/c			1,60,000
	To Security Premium Reserve A/c			30,000
	(2,000 Forfeited shares reissued for ₹95 per share ₹80 paid up)			
	Share Forfeited A/c[3] Dr.		92,000	
	To Capital Reserve A/c			92,000
	(Gain on forfeiture transferred to capital reserve)			

Working Notes :

(1) (A) Excess amount received from Dhwani on application :

Dhwani has been allotted 1,600 shares.

$$\text{Shares applied by Dhwani} = 1{,}600 \times \frac{1{,}20{,}000}{80{,}000} = 2{,}400$$

Excess application money received from Dhwani :

2,400 Shares – 1,600 Shares = 800 Shares × ₹30 = ₹24,000

(B) Amount due from Dhwani on allotment :

		₹
1,600 × ₹30	=	48,000
Less : Excess received from Dhwani on application	=	24,000
Net amount due from Dhwani on allotment, which has not been received	=	24,000

(C)

Total amount due on allotment 80,000 Shares × ₹30	=	24,00,000
Less : Excess amount received on applications	=	12,00,000
Balance Due	=	12,00,000
Less : Amount not received from Dhwani on allotment	=	24,000
Net amount received on allotment in Cash		11,76,000

(2) Calls in Arrear on First Call :

From Dhwani : 1,600 × ₹30	48,000
From Sargam (Who has been allotted $6{,}000 \times \frac{80{,}000}{1{,}20{,}000} = 4{,}000$ shares)	
4,000 × ₹30	1,20,000
	1,68,000

(3) Transfer to Capital Reserve :

	₹
Forfeited amount on 1,600 shares of Dhwani Since she has applied for 2,400 shares and has paid application money of ₹30 per share, forfeited amount will be : 2,400 × ₹30	72,000
Forfeited amount on 400 shares of Sargam : Sargam has paid ₹30 on application and ₹20 (excluding premium) on allotment	
400 shares × ₹50	20,000
Transferred to Capital Reserve	92,000

ILLUSTRATION 49.

Anishka Ltd. invited applications for 2,00,000 equity shares of ₹10 each at a premium of ₹4 per share. The amount was payable as follows :

On Application	₹6 (including premium ₹2)
On Allotment	₹7 (including premium ₹2)
Balance on first and final call.	

Applications for 3,00,000 shares were received. Allotment was made to all the applicants on pro-rata basis.

Mehak, to whom 400 shares were allotted failed to pay allotment and call money. Khushboo, who had applied for 300 shares failed to pay the call money. Their shares were forfeited after final call. 400 of the forfeited shares (including all shares of Khushboo) were reissued @ ₹8 per share as fully paid up.

Pass the necessary journal entries by opening 'Calls in Arrears A/c' wherever necessary. *(C.B.S.E. Sample Paper, 2019)*

SOLUTION : BOOKS OF ANSHIKA LTD.

Date	*Particulars*		*L.F.*	*Dr. (₹)*	*Cr. (₹)*
	Bank A/c	Dr.		18,00,000	
	To Equity Share Application A/c				18,00,000
	(Application money received for 3,00,000 shares)				
	Equity Share Application A/c	Dr.		18,00,000	
	To Equity Share Capital A/c				8,00,000
	To Securities Premium Reserve A/c				4,00,000
	To Equity Share Allotment A/c				6,00,000
	(2,00,000 shares allotted and excess amount credited to Share Allotment A/c)				
	Equity Share Allotment A/c	Dr.		14,00,000	
	To Equity Share Capital A/c				10,00,000
	To Securities Premium Reserve A/c				4,00,000
	(Allotment money due on 2,00,000 shares)				

Bank A/c[1]	Dr.	7,98,400	
Calls in Arrears A/c	Dr.	1,600	
To Equity Share Allotment A/c			8,00,000
(Allotment money received on 1,99,600 Shares)			
Equity Share First & Final Call A/c	Dr.	2,00,000	
To Equity Share Capital A/c			2,00,000
(Call money due on 2,00,000 shares @ ₹1 per share)			
Bank A/c	Dr.	1,99,400	
Calls in Arrears A/c (600 × ₹1)[2]	Dr.	600	
To Equity Share First & Final Call A/c			2,00,000
(Call money received on 1,99,400 shares)			
Equity Share Capital A/c	Dr.	6,000	
Securities Premium Reserve A/c[3]	Dr.	800	
To Calls in Arrears A/c			2,200
To Share Forfeiture A/c			4,600
(Forfeiture of 600 shares)			
Bank A/c	Dr.	3,200	
Share Forfeiture A/c	Dr.	800	
To Equity Share Capital A/c			4,000
(Re-issue of 400 shares @ ₹8 per share)			
Share Forfeiture A/c	Dr.	2,400	
To Capital Reserve A/c[4]			2,400
(Gain on reissue of forfeited shares transferred to Capital Reserve Account)			

Working Notes :

(1) (A) Excess amount received from Mehak on application :

Mehak has been allotted 400 shares.

She must have applied for $\frac{3,00,000}{2,00,000} \times 400 = 600$ Shares.

Excess application money received from Mehak = 600 Shares – 400 Shares
= 200 Shares × ₹6 = ₹1,200

(B) Amount due from Mehak on Allotment :

		₹
400 Shares × ₹7	=	2,800
Less : excess received from Mehak on application	=	1,200
Allotment money not received from Mehak		1,600

(C)

Total amount due on allotment : 2,00,000 shares × ₹7	=	14,00,000
Less : Excess amount received on application	=	6,00,000
Balance Due		8,00,000
Less : Amount not received from Mehak on Allotment		1,600
Net amount received on allotment in Cash		7,98,400

(2) Khushboo, who had applied for 300 shares must have been allotted $300 \times \frac{2,00,000}{3,00,000} =$ 200 shares. Hence, First and Final Call is not received on 400 shares of Mehak + 200 shares of Khushboo.

(3) Mehak has not paid allotment money on her 400 shares. Hence, Securities Premium Reserve has been debited on the amount of premium not received on her 400 shares @ ₹2 each.

(4) Amount transferred to Capital Reserve :
400 shares have been reissued which include 200 shares of Mehak and 200 shares of Khushboo.

			₹
(*i*) Mehak has paid application money on 600 shares @ ₹6 each	=		3,600
Less : Amount of premium adjusted on application : 400 shares @ ₹2 each			800
			2,800

This excess amount of ₹2,800 is the amount forfeited on her 400 shares.

Forfeited amount on her 200 shares = $2{,}800 \times \frac{200}{400}$	=		1,400
(*ii*) Forfeited amount on Khushboo's 200 shares :			
Amount paid on Application : 200 × ₹4 (excluding premium)		800	
Amount paid on Allotment : 200 × ₹5 (excluding premium)		1,000	1,800
			3,200
Less : Loss on Reissue : 400 shares × ₹2			800
Amount transferred to Capital Reserve			2,400

ILLUSTRATION 50.

KS Ltd. invited applications for issuing 1,60,000 equity shares of ₹10 each at a premium of ₹6 per share. The amount was payable as follows :

On Application — ₹4 per share (including premium ₹1 per share)
On Allotment — ₹6 per share (including premium ₹3 per share)
On First and Final Call — Balance.

Applications for 3,20,000 shares were received. Applications for 80,000 shares were rejected and application money refunded. Shares were allotted on pro-rata basis to the remaining applicants. Excess money received with applications was adjusted towards sums due on allotment. Jain holding 800 shares, failed to pay the allotment money. His shares were forfeited immediately after allotment. Afterwards the final call was made. Gupta who had applied for 1,200 shares failed to pay the final call. These shares were also forfeited. Out of the forfeited shares 1,000 shares were re-issued at ₹8 per share fully paid up. The re-issued shares included all the forfeited shares of Jain.

Pass necessary Journal entries for the above transactions in the books of KS Ltd.
(C.B.S.E, 2016, Delhi)

SOLUTION :

JOURNAL OF *KS* LTD.

Date	*Particulars*		*L.F.*	*Dr. Amount*	*Cr. Amount*
				₹	₹
	Bank A/c (3,20,000 × ₹4)	Dr.		12,80,000	
	To Equity Share Application A/c				12,80,000
	(Application money received on 3,20,000 shares)				

Equity Share Application A/c	Dr.	12,80,000	
To Equity Share Capital A/c (1,60,000 × ₹3)			4,80,000
To Securities Premium Reserve A/c (1,60,000 × ₹1)			1,60,000
To Equity Share Allotment A/c (80,000 × ₹4)			3,20,000
To Bank A/c (80,000 × ₹4)			3,20,000
(Application money adjusted & surplus refunded)			
Equity Share Allotment A/c	Dr.	9,60,000	
To Equity Share Capital A/c			4,80,000
To Securities Premium Reserve A/c			4,80,000
(Share allotment made due)			
Bank A/c(1)	Dr.	6,36,800	
Calls in Arrears A/c	Dr.	3,200	
To Equity Share Allotment A/c			6,40,000
(Allotment money received except on 800 shares)			
Equity Share Capital A/c (800 × ₹6)	Dr.	4,800	
Securities Premium Reserve A/c (800 × ₹3)	Dr.	2,400	
To Calls in Arrears A/c			3,200
To Forfeited Shares A/c			4,000
(800 shares of Jain forfeited after allotment)			
Equity Share First & Final Call A/c (1,59,200 × ₹6)	Dr.	9,55,200	
To Equity Share Capital A/c (1,59,200 × ₹4)			6,36,800
To Securities Premium Reserve A/c (1,59,200 × ₹2)			3,18,400
(First & final call due on 1,59,200 shares)			
Bank A/c (1,58,400 × ₹6)	Dr.	9,50,400	
Calls in Arrears A/c	Dr.	4,800	
To Equity Share First & Final Call A/c			9,55,200
(First & final call money received except on 800 shares held by Gupta)			
Equity Share Capital A/c (800 × ₹10)	Dr.	8,000	
Securities Premium Reserve A/c (800 × ₹2)	Dr.	1,600	
To Calls in Arrears A/c (800 × ₹6)			4,800
To Forfeited Shares A/c			4,800
(800 shares of Gupta forfeited for non-payment of call money)			
Bank A/c	Dr.	8,000	
Forfeited Shares A/c	Dr.	2,000	
To Equity Share Capital A/c			10,000
(1,000 shares reissued @₹8 per share fully paid up)			
Forfeited Shares A/c	Dr.	3,200	
To Capital Reserve A/c(3)			3,200
(Gain on reissue of forfeited shares transferred to capital reserve)			

Working Notes :

(1) (*a*) Total Number of shares applied by Jain = $800 \times \frac{2,40,000}{1,60,000} = 1,200$ shares

Excess application money received :
1,200 shares – 800 shares = 400 shares × ₹4 = ₹1,600

(*b*)	
Allotment money due from Jain = 800 × ₹6	₹4,800
Less : Excess received on application stage	₹1,600
Allotment money not received	₹3,200

(*c*)	
Total amount due on allotment : 1,60,000 shares × ₹6	9,60,000
Less : Excess received on application	3,20,000
	6,40,000
Less : Amount not received from Jain on allotment	3,200
Net Amount received on allotment in cash	6,36,800

(2) Gupta was allotted = $1,200 \times \frac{1,60,000}{2,40,000} = 800$ shares

(3) Calculation of Gain on Re-issue to be transferred to Capital Reserve :

Amount forfeited on Re-issued shares	
Jain (800 shares)	₹4,000
Gupta (200 shares) $\left[₹4,800 \times \frac{200}{800}\right]$	₹1,200
Total Forfeited amount on 1,000 shares	₹5,200
Less : Discount on Re-issue	₹2,000
Gain on Re-issue to be transferred to Capital Reserve	₹3,200

ILLUSTRATION 51.

Rajesh Ltd. issued a prospectus inviting applications for 3,00,000 shares of ₹10 each at a premium of ₹4 per share, payable as follows :

On Application	₹4 (including ₹1 premium)
On Allotment	₹3 (including ₹1 premium)
On First Call	₹4 (including ₹1 premium)
On Second & Final Call	₹3 (including ₹1 premium)

Applications were received for 3,80,000 shares and pro-rata allotment was made on the applications for 3,50,000 shares. It was decided to utilise excess application money towards the sums due on allotment.

X, to whom 6,000 shares were allotted, failed to pay the allotment money and his shares were forfeited after allotment.

Y, who applied for 10,500 shares failed to pay the two calls and on his such failure, his shares were forfeited.

Z, who was allotted 3,000 shares did not pay final call.

Of the shares forfeited, 11,000 shares were reissued as fully paid up for ₹9 per share, the whole of *Y*'s shares being included. Prepare Cash Book, Journal and Balance Sheet.

SOLUTION :

RAJESH LTD.
CASH BOOK

Dr. Cr.

Particulars	₹	*Particulars*	₹
To Share Application A/c		By Share Application A/c	
(3,80,000 shares × ₹4)	15,20,000	(30,000 Shares × ₹4)	1,20,000
To Share Allotment A/c(4)	6,86,000	By Balance c/d	41,71,000
To Share First Call A/c			
(2,85,000 Shares × ₹4)(5)	11,40,000		
To Share Second & Final Call A/c (2,82,000 Shares × ₹3)(5)	8,46,000		
To Share Capital A/c	99,000		
	42,91,000		42,91,000

JOURNAL

Date	*Particulars*		*L.F.*	*Dr.* ₹	*Cr.* ₹
	Share Application A/c	Dr.		14,00,000	
	To Share Capital A/c (3,00,000 shares × ₹3)				9,00,000
	To Securities Premium Reserve A/c (3,00,000 shares × ₹1)				3,00,000
	To Share Allotment A/c (50,000 shares × ₹4)				2,00,000
	(Application money transferred)				
	Share Allotment A/c	Dr.		9,00,000	
	To Share Capital A/c				6,00,000
	To Securities Premium Reserve A/c				3,00,000
	(Allotment due on 3,00,000 shares)				
	Calls in Arrears A/c	Dr.		14,000	
	To Share Allotment A/c				14,000
	(Allotment money not received from *X* on his 6,000 shares)				
	Share Capital A/c (6,000 shares × ₹5)	Dr.		30,000	
	Securities Premium Reserve A/c (6,000 shares × ₹1 due on allotment)	Dr.		6,000	
	To Calls in Arrears A/c				14,000
	To Share Forfeiture A/c				22,000
	(Forfeiture of 6,000 shares of *X* for non payment of allotment money)				
	Share First Call A/c	Dr.		11,76,000	
	To Share Capital A/c				8,82,000
	To Securities Premium Reserve A/c				2,94,000
	(Provisions of premium on 2,94,000 shares)				
	Calls in Arrears A/c	Dr.		36,000	
	To Share First Call A/c				36,000
	(First call not received from *Y* on his 9,000 shares)				

Share Second & Final Call A/c	Dr.		8,82,000	
To Share Capital A/c				5,88,000
To Securities Premium Reserve A/c				2,94,000
(Second & final call due on 2,94,000 shares)				
Calls in Arrears A/c	Dr.		36,000	
To Share Second & Final Call A/c				36,000
(Final call not received on *Y*'s 9,000 shares and *Z*'s 3,000 shares)				
Share Capital A/c	Dr.		90,000	
Securities Premium Reserve A/c	Dr.		18,000	
To Calls in Arrears A/c				63,000
To Share Forfeiture A/c				45,000
(Forfeiture of 9,000 shares of *Y* for non payment of calls)				
Share Forfeiture A/c	Dr.		11,000	
To Share Capital A/c				11,000
(Loss of ₹1 per share on the re-issue of 11,000 shares)				
Share Forfeiture A/c(6)	Dr.		41,333	
To Capital Reserve A/c				41,333
(Gain on 11,000 re-issued shares transferred to capital reserve)				

BALANCE SHEET OF RAJESH LTD.

as at ....

Particulars	*Note No.*	*Current year*	*Previous year*
I. EQUITY AND LIABILITIES :		₹	₹
Shareholder's Funds :			
(*a*) Share Capital	1	29,68,667	
(*b*) Reserve and Surplus	2	12,02,333	
		41,71,000	
II. ASSETS :			
Current Assets :			
Cash and Bank Balance	3	41,71,000	

Notes to Accounts :

		₹	₹
(1) **Share Capital :**			
Authorised :			
.....Shares of ₹10 each		....	
Issued :			
3,00,000 Shares of ₹10 each		30,00,000	
Subscribed and Fully Paid Capital:			
2,93,000 Shares of ₹10 each	29,30,000		

Subscribed but not Fully Paid Capital :			
3,000 Shares of ₹10 each	30,000		
Less : Calls in Arrears (3,000 Shares × ₹2)	6,000	24,000	
		29,54,000	
Add : Share Forfeiture A/c$^{(7)}$		14,667	29,68,667
(2) **Reserve and Surplus :**			
Capital Reserve			41,333
Securities Premium Reserve		11,64,000	
Less : Calls in Arrears (3,000 Shares × ₹1)		3,000	11,61,000
			12,02,333
(3) **Cash and Bank Balance :**			
Cash at Bank			41,71,000

(4) (A) Excess amount received from *X* on application :

X has been allotted 6,000 shares

Therefore, he must have applied for $\frac{3,50,000}{3,00,000} \times 6,000 = 7,000$ shares.

Excess application money received from *X* :

7,000 Shares – 6,000 Shares = 1,000 Shares × ₹4 = ₹4,000.

(B) Amount due from *X* on Allotment :	₹
6,000 Shares × ₹3	18,000
Less : Excess received from *X* on Application	4,000
Allotment money not received from *X*	14,000

(C) Total amount due on Allotment : 3,00,000 Shares × ₹3	9,00,000
Less : Excess amount received on Application	2,00,000
Balance Due	7,00,000
Less : Amount not received from *X* on Allotment	14,000
Net amount received on Allotment in Cash	6,86,000

(5) *Y* has applied for 10,500 shares.

Therefore, he must have been allotted $\frac{3,00,000}{3,50,000} \times 10,500 = 9,000$ Shares.

He has not paid first and second call money.

As such, (*i*) First Call money will be received on 2,94,000 shares – 9,000 shares of *Y* = 2,85,000 shares.

(*ii*) Second Call money will be received on 2,94,000 shares – 9,000 shares of *Y* – 3,000 shares of *Z* = 2,82,000 shares.

(6) 11,000 shares have been re-issued which include 9,000 shares of *Y* and the balance 2,000 of *X*.

		₹
Forfeited amount on 2,000 shares of $X = \frac{₹22,000}{6,000 \text{ Shares}} \times 2,000$ Shares	=	7,333
Forfeited amount on 9,000 shares of *Y*	=	45,000
		52,333
Less : Loss on re-issue of 11,000 shares @ ₹1 each		11,000
		41,333

(7) Balance in Share Forfeiture A/c :

Forfeited amount on 6,000 shares of *X* = 22,000

Therefore, the balance of Share Forfeiture A/c on 4,000 un-issued shares $= \dfrac{₹22{,}000}{6{,}000 \text{ Shares}} \times 4{,}000 \text{ Shares} = ₹14{,}667.$

ILLUSTRATION 52.

Cargo Ltd. invited applications for the issue of 20,000 Equity Shares of ₹10 each at a premium of ₹1 per share, payable as follows :

On Application	₹3
On Allotment	The balance (including premium ₹1)

Applications were received for 30,000 shares and pro-rata allotment was made to the remaining applicants after refunding application money to 5,000 share applicants.

Nicholas, who was allotted 3,000 shares, failed to pay the allotment money and his shares were forfeited.

Out of these forfeited shares, 1,000 shares were reissued as fully paid-up @ ₹8 per share.

You are required to :

(*i*) Pass journal entries in the books of the company.

(*ii*) Prepare Calls-in-arrears Account.

(*iii*) Prepare Share Forfeiture Account. *(I.S.C. 2017)*

SOLUTION :

Journal of Cargo Ltd.

Date	*Particulars*		*L.F.*	*Dr.* (₹)	*Cr.* (₹)
	Bank A/c	Dr.		90,000	
	To Share Application A/c				90,000
	(Share application money received)				
	Share Application A/c	Dr.		90,000	
	To Equity Share Capital A/c				60,000
	To Share Allotment A/c				15,000
	To Bank A/c				15,000
	(Share application money transferred)				
	Share Allotment A/c	Dr.		1,60,000	
	To Equity Share Capital A/c				1,40,000
	To Securities Premium Reserve A/c				20,000
	(Share allotment due)				
	Bank A/c	Dr.		1,23,250	
	Calls in Arrears A/c	Dr.		21,750	
	To Share Allotment A/c				1,45,000
	(Share allotment received on 17,000 shares)				
	Equity Share Capital A/c	Dr.		30,000	
	Securities Premium Reserve A/c	Dr.		3,000	
	To Calls in Arrear A/c				21,750
	To Share Forfeiture A/c				11,250
	(3,000 shares forfeited)				

	Bank A/c Dr.		8,000	
	Share Forfeiture A/c Dr.		2,000	
	To Equity Share Capital A/c			10,000
	(1,000 shares reissued)			
	Share Forfeiture A/c Dr.		1,750	
	To Capital Reserve A/c			1,750
	(Transfer of net gain on 1,000 reissued shares to Capital Reserve)			

Dr. **CALLS-IN-ARREARS A/C** Cr.

Particulars	*J.F.*	₹	*Particulars*	*J.F.*	₹
To Share Allotment A/c		21,750	By Securities Premium Reserve		3,000
			By Equity Share Capital		18,750
		21,750			21,750

Dr. **SHARE FORFEITURE A/C** Cr.

Particulars	*J.F.*	₹	*Particulars*	*J.F.*	₹
To Equity Share Capital A/c		2,000	By Equity Share Capital A/c		11,250
To Capital Reserve A/c		1,750			
To Balance c/d		7,500			
		11,250			11,250

Working Notes :

(1) (A) Nicholas must have applied for $3,000 \times \frac{25,000}{20,000} = 3,750$ shares

Excess amount = 3,750 shares – 3,000 shares = 750 shares × ₹3 = ₹2,250

(B)

	₹
Amount due from Nicholas on allotment : 3,000 × ₹8	24,000
Less : Excess received from him on application	2,250
	21,750

(C)

	₹
Total amount due on allotment : 20,000 × ₹8	1,60,000
Less : Excess received on application : 5,000 × ₹3	15,000
	1,45,000
Less : Not received from Nicholas on allotment	21,750
	1,23,250

(2) Amount transferred to Capital Reserve : ₹

Amount forfeited on 3,000 shares = 11,250

∴ Amount forfeited on 1,000 shares = $\frac{11,250}{3,000} \times 1,000$ = 3,750

Less : Loss on Reissue 2,000

1,750

ILLUSTRATION 53.

Manvet Ltd. invited applications for issuing 10,00,000 equity shares of ₹10 each payable as follows :

On application and allotment ₹4 per share (including premium ₹1),
On first call ₹4 per share,
On second and final call ₹3 per share.

Applications for 15,00,000 shares were received and pro-rata allotment was made to all the applicants. Excess application money was adjusted on the sums due on calls. A shareholder who had applied for 6,000 shares did not pay the first, and the second and final call. His shares were forfeited. 90% of the forfeited shares were reissued at ₹8 per share fully paid up.

Pass necessary journal entries for the above transactions in the books of the company. *(C.B.S.E. 2018, Comptt.)*

SOLUTION :

Books of Manvet Ltd.

JOURNAL

Date	*Particulars*		*L.F.*	*Dr. (₹)*	*Cr. (₹)*
(*i*)	Bank A/c	Dr.		60,00,000	
	To Equity Share Application & Allotment A/c				60,00,000
	(Application money received on 15,00,000 shares)				
(*ii*)	Equity Share Application & Allotment A/c	Dr.		60,00,000	
	To Equity Share Capital A/c				30,00,000
	To Securities Premium Reserve A/c				10,00,000
	To Calls in Advance A/c				20,00,000
	(Application & Allotment money adjusted)				
(*iii*)	Equity Share First Call A/c	Dr.		40,00,000	
	To Equity Share Capital A/c				40,00,000
	(First call money due on 10,00,000 shares)				
(*iv*)	Bank A/c(1)	Dr.		19,92,000	
	Calls in arrear A/c	Dr.		8,000	
	Calls in Advance A/c	Dr.		20,00,000	
	To Equity Share First Call A/c				40,00,000
	(First call money received except on 4,000 shares and calls in advance adjusted)				
(*v*)	Equity Share Second & Final Call A/c	Dr.		30,00,000	
	To Equity Share Capital A/c				30,00,000
	(Second & Final Call money due on 10,00,000 shares)				
(*vi*)	Bank A/c	Dr.		29,88,000	
	Calls in arrear A/c	Dr.		12,000	
	To Equity Share Second & Final Call A/c				30,00,000
	(Second and final call money received except on 4,000 shares)				

(vii)	Equity Share Capital A/c Dr.		40,000	
	To Calls-in-Arrear A/c			20,000
	To Forfeited Shares A/c			20,000
	(Forfeiture of 4,000 shares for non payment of call money)			
(viii)	Bank A/c Dr.		28,800	
	Forfeited Shares A/c Dr.		7,200	
	To Equity Share Capital A/c			36,000
	(3,600 of the forfeited shares reissued as fully paid up)			
(ix)	Forfeited Shares A/c(2) Dr.		10,800	
	To Capital Reserve A/c			10,800
	(Gain on 3,600 reissued shares transferred to capital reserve A/c)			

Working Notes :

(1) (A) Applicant for 6,000 shares must have been allotted $\frac{10,00,000}{15,00,000} \times 6,000$

= 4,000 shares

Excess amount received from him on application

= 6,000 Shares – 4,000 Shares = 2,000 Shares × ₹4 = ₹8,000

		₹
(B) Amount due from him on first call (4,000 × ₹4)	=	16,000
Less : Excess received from him on application	=	8,000
Amount not paid on first call		8,000
(C) Total amount due on First Call : 10,00,000 Shares × ₹4	=	40,00,000
Less : Excess amount received on Application		20,00,000
		20,00,000
Less : Not received on First Call		8,000
Net amount received on First Call		19,92,000

(2) Amount transferred to Capital Reserve :

Amount forfeited on 4,000 Shares = 20,000

∴ Amount forfeited on 3,600 Shares = $20,000 \times \frac{3,600}{4,000}$ = 18,000

Less : Loss on Re-issue 7,200

Transferred to Capital Reserve 10,800

ILLUSTRATION 54.

A limited company forfeited 300 shares of Mr. *X* who had applied for 500 shares on account of non-payment of allotment money ₹3 + 2 (premium) and first call ₹2. Only ₹3 per share was received with application. Out of these, 200 shares were re-issued to Mr. *Y* as fully paid in such a way that ₹600 were transferred to capital reserve.

Give journal entries relating to forfeiture and re-issue.

SOLUTION :

JOURNAL

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
	Share Capital Account	Dr.		2,400	
	Securities Premium Reserve A/c	Dr.		600	
	To Share Allotment Account(1)				900
	To Share First Call Account				600
	To Share Forfeiture Account				1,500
	(Forfeiture of 300 shares for non-payment of allotment money and first call money, the shares being ₹8 called up, each)				
	Bank Account(2)	Dr.		1,600	
	Share Forfeiture Account	Dr.		400	
	To Share Capital Account				2,000
	(Re-issue of 200 shares @ ₹8 per share, fully paid up)				
	Share Forfeiture Account	Dr.		600	
	To Capital Reserve Account				600
	(Transfer to Capital Reserve)				

Working Notes :

(1) Excess Application money received from *X* :

		₹
500 Shares – 300 Shares = 200 Shares × ₹3	=	600
Amount due from *X* on allotment 300 Shares × ₹5	=	1,500
Less : Excess received from *X* on application		600
Amount not paid on allotment		900

(2) Amount transferred to Capital Reserve :

			₹
Amount forfeited on 300 Shares	=	₹1,500	
∴ Amount forfeited on 200 Shares	=	$1{,}500 \times \frac{200}{300}$	1,000
Less : Transferred to Capital Reserve			600
Loss on Re-issue			400

Per Share Loss on Re-issue = $\frac{₹400}{200}$ = ₹2 per share.

Re-issue price = ₹10 – ₹2 = ₹8 per share.

ILLUSTRATION 55.

XY Ltd. invited applications for issuing 50,000 equity shares of ₹10 each. The amount was payable as follows :

On Application	₹3 per share
On Allotment	₹4 per share
On First and Final Call	₹3 per share

Applications were received for 75,000 shares and pro-rata allotment was made as follows :

Applicants for 40,000 shares were allotted 30,000 shares on pro-rata basis.

Applicants for 35,000 shares were allotted 20,000 shares on pro-rata basis.

Ramu, to whom 1,200 shares were allotted out of the group applying for 40,000 shares failed to pay the allotment money. His shares were forfeited immediately after allotment.

Shamu, who had applied for 700 shares out of the group applying for 35,000 shares failed to pay the first and final call. His shares were also forfeited. Out of the forfeited shares 1,000 shares were re-issued @ ₹8 per share fully paid up. The re-issued shares included all the forfeited shares of Shamu.

Pass necessary journal entries to record the above transactions.

SOLUTION :

XY LTD.

JOURNAL

Date	*Particulars*		*L.F.*	*Dr.*	*Cr.*
				₹	₹
	Bank A/c	Dr.		2,25,000	
	To Share Application A/c				2,25,000
	(Application money received on 75,000 shares)				
	Share Application A/c	Dr.		2,25,000	
	To Share Capital A/c				1,50,000
	To Share Allotment A/c				75,000
	(Application money adjusted)				
	Share Allotment A/c	Dr.		2,00,000	
	To Share Capital A/c				2,00,000
	(Allotment money due)				
	Bank A/c(1)	Dr.		1,21,400	
	Calls in Arrears A/c	Dr.		3,600	
	To Share Allotment A/c				1,25,000
	(Allotment money received on 48,800 shares)				
	Share Capital A/c	Dr.		8,400	
	To Calls in Arrears A/c				3,600
	To Share Forfeiture A/c				4,800
	(1,200 shares forfeited for non-payment of allotment money)				
	Share First and Final Call A/c	Dr.		1,46,400	
	To Share Capital A/c				1,46,400
	(First and final call due on 48,800 shares)				
	Bank A/c(2)	Dr.		1,45,200	
	Calls in Arrears A/c	Dr.		1,200	
	To Share First and Final Call A/c				1,46,400
	(First and final call money received on 48,400 shares)				
	Share Capital A/c	Dr.		4,000	
	To Calls in Arrears A/c				1,200
	To Share Forfeiture A/c				2,800
	(400 shares forfeited for non-payment of first and final call)				

	Bank A/c	Dr.	8,000	
	Share Forfeiture A/c	Dr.	2,000	
	To Share Capital A/c			10,000
	(Re-issue of 1,000 shares @ ₹8 per share as fully paid-up)			
	Share Forfeiture A/c	Dr.	3,200	
	To Capital Reserve A/c			3,200
	(Transfer of gain on re-issue)			

Working Notes :

(1) (A) Ramu must have applied for $\frac{40,000}{30,000} \times 1,200 = 1,600$ Shares

Excess amount received from Ramu on application = 1,600 shares – 1,200 shares
= 400 shares × ₹3 = ₹1,200

	₹
(B) Amount due from Ramu on allotment	4,800
Less : Excess received from Ramu on application	1,200
	3,600

(C) Total amount due on allotment : 50,000 shares × ₹4	2,00,000
Less : Excess received on application	75,000
	1,25,000
Less : Not received from Ramu on allotment	3,600
	1,21,400

(2) Calculation of No. of shares allotted to Shamu :

$$\frac{20,000}{35,000} \times 700 = 400 \text{ shares}$$

It means Shamu has not paid first and final call money on 400 shares.

(3) Calculation of amount to be transferred to Capital Reserve :
Only 1,000 shares have been re-issued which include all the shares of Shamu. Hence all the 400 shares of Shamu and only 600 shares of Ramu have been re-issued.

	₹
Amount forfeited on 400 shares of Shamu	2,800
Amount forfeited on 600 shares of Ramu = $\frac{₹4,800}{1,200 \text{ shares}} \times 600$ shares	2,400
	5,200
Less : Loss on re-issue of 1,000 shares @ ₹2 each	2,000
	3,200

ILLUSTRATION 16.

X Ltd. invited applications for issuing 2,00,000 equity shares of ₹10 each. The amount was payable as follows :

	₹
On Application	2.50
On Allotment	5
On First and Final Call	2.50

Applications for 3,50,000 Shares were received and the allotment was made as follows :

Category	*Shares applied for*	*Shares allotted*
I	50,000	40,000
II	1,00,000	60,000
III	2,00,000	1,00,000

All the shares were allotted on *pro-rata* basis and excess application money was adjusted towards sum due on allotment.

Madhu, who belonged to category I and to whom 800 shares were allotted, failed to pay the allotment money. Her shares were forfeited immediately after allotment was not received. Pooja, who belonged to category III and who had applied for 400 shares, failed to pay the final call money. Her shares were forfeited after the final call. The forfeited shares were re-issued @ ₹9 per share fully paid up.

Pass necessary Journal entries in the books of *X* Ltd.

SOLUTION : JOURNAL OF *X* LTD.

Date	*Particulars*		*L.F.*	*Dr.*	*Cr.*
				₹	₹
	Bank A/c	Dr.		8,75,000	
	To Equity Share Application A/c				8,75,000
	(Application money received on 3,50,000 shares)				
	Equity Share Application A/c	Dr.		8,75,000	
	To Equity Share Capital A/c				5,00,000
	To Equity Share Allotment A/c(1)				3,75,000
	(Application money adjusted)				
	Equity Share Allotment A/c	Dr.		10,00,000	
	To Equity Share Capital A/c				10,00,000
	(Allotment money due on 2,00,000 shares @ ₹5 each)				
	Bank A/c(2)	Dr.		6,21,500	
	Calls in Arrears A/c	Dr.		3,500	
	To Equity Share Allotment A/c				6,25,000
	(Allotment money received on 1,99,200 shares)				
	Equity Share Capital	Dr.		6,000	
	To Calls in Arrears A/c				3,500
	To Share Forfeiture A/c				2,500
	(800 shares forfeited for non payment of allotment money)				
	Equity Share First & Final Call A/c	Dr.		4,98,000	
	To Equity Share Capital A/c				4,98,000
	(First and final call due on 1,99,200 shares)				
	Bank A/c	Dr.		4,97,500	
	Calls in Arrears A/c	Dr.		500	
	To Equity Share First & Final Call A/c				4,98,000
	(First and final call money received except on 200 shares of Pooja)				

	Equity Share Capital A/c Dr.		2,000	
	To Calls in Arrears A/c			500
	To Share Forfeiture A/c			1,500
	(200 shares of Pooja forfeited for non-payment of first and final call)			
	Bank A/c Dr.		9,000	
	Share Forfeiture A/c Dr.		1,000	
	To Equity Share Capital A/c			10,000
	(1,000 shares re-issued @ ₹9 each fully paid up)			
	Share Forfeiture A/c Dr.		3,000	
	To Capital Reserve A/c			3,000
	(Transfer of gain on re-issue)			

Working Notes :

(1) Calculation of excess application money adjusted on allotment :

Category	*Shares Applied*	*Shares Allotted*		*Excess amount received on application* ₹	*Amount adjusted on allotment* ₹	*Amount returned* ₹
I	50,000	40,000	10,000 shares @ ₹2.50	25,000	25,000	—
II	1,00,000	60,000	40,000 shares @ ₹2.50	1,00,000	1,00,000	—
III	2,00,000	1,00,000	1,00,000 shares @ ₹2.50	2,50,000	2,50,000	—
	3,50,000	2,00,000		3,75,000	3,75,000	—

(2) (A) Madhu must have applied for $\frac{50,000}{40,000} \times 800 = 1,000$ shares.

Excess amount received from Madhu on application = 1,000 shares – 800 shares
= 200 shares × ₹2.50 = ₹500

		₹
(B) Amount due from Madhu on allotment : 800 shares @ ₹5	=	4,000
Less : Excess received from Madhu on application		500
		3,500

		₹
(C) Total amount due on allotment : 2,00,000 shares × ₹5	=	10,00,000
Less : Excess received on application		3,75,000
		6,25,000
Less : Not received from Madhu on allotment		3,500
		6,21,500

(3) Calculation of No. of shares allotted to Pooja : $\frac{1,00,000}{2,00,000} \times 400 = 200$ shares

It means Pooja has not paid first and final call money on 200 shares.

ILLUSTRATION 57.

Sudarshan Ltd. invited applications for 1,00,000 Equity Shares of ₹10 each. The shares were issued at a premium of ₹5 per share. The amount was payable as follows:

On application and allotment ₹8 per share (including premium ₹3).

Balance including premium on the first and final call.

Applications for 1,50,000 shares were received. Applications for 10,000 shares were rejected and pro-rata allotment was made to the remaining applicants on the following basis:

(*i*) Applicants for 80,000 shares were allotted 60,000 shares ; and

(*ii*) Applicants for 60,000 shares were allotted 40,000 shares.

Excess share application and allotment money could be utilized for calls.

X, who belonged to the first category and was allotted 300 shares, failed to pay the first call money. *Y*, who belonged to the second category and was allotted 200 shares also failed to pay the first call money. Their shares were forfeited. The forfeited shares were re-issued @ ₹12 per share fully paid-up.

Pass necessary Cash-Book and Journal entries. *(C.B.S.E. 2019, Kerala)*

SOLUTION :

Sudarshan Ltd.

CASH BOOK

Dr. Cr.

Particulars	₹	*Particulars*	₹
To Equity Share Application and Allotment A/c (1,50,000 shares × ₹8)	12,00,000	By Equity Share Application and Allotment A/c (Refund of applications for 10,000 shares @ ₹8 per share)	80,000
To Equity Share First and Final Call A/c (₹7,00,000 – ₹3,20,000 – ₹1,900)(1)	3,78,100	By Balance c/d	15,04,100
To Equity Share Capital A/c	5,000		
To Securities Premium Reserve A/c	1,000		
	15,84,100		15,84,100

JOURNAL

Date	*Particulars*		*L.F.*	*Dr.* ₹	*Cr.* ₹
	Equity Share Application and Allotment A/c	Dr.		11,20,000	
	To Equity Share Capital A/c (1,00,000 × ₹5)				5,00,000
	To Securities Premium Reserve A/c (1,00,000 × ₹3)				3,00,000
	To Calls in Advance A/c (40,000 × ₹8)				3,20,000
	(Transfer of application and allotment money)				
	Equity Share First & Final Call A/c	Dr.		7,00,000	
	To Equity Share Capital A/c				5,00,000
	To Securities Premium Reserve A/c				2,00,000
	(First & Final Call due on 1,00,000 shares)				
	Calls in Arrears A/c	Dr.		1,900	
	To Equity Share First & Final Call A/c				1,900
	(Amount not received on call)				

	Calls in Advance A/c Dr.		3,20,000	
	To Equity Share First & Final Call A/c			3,20,000
	(Calls in Advance adjusted to Share First & Final Call A/c)			
	Equity Share Capital A/c (500 × ₹10) Dr.		5,000	
	Securities Premium Reserve A/c (500 × ₹2) Dr.		1,000	
	To Calls in Arrears A/c (₹1,300 + ₹600)			1,900
	To Share Forfeiture A/c			4,100
	(Forfeiture of 300 shares of *X* and 200 shares of *Y* for non- payment of call money)			
	Share Forfeiture A/c Dr.		4,100	
	To Capital Reserve A/c			4,100
	(Balance of share forfeiture transferred to capital reserve)			

Working Notes :

(1) (A) No. of shares applied by *X* $= \frac{80,000}{60,000} \times 300 = 400$

No. of shares applied by *Y* $= \frac{60,000}{40,000} \times 200 = 300$

Excess amount received from *X* = 400 Shares – 300 Shares
= 100 Shares × ₹8 = ₹800

Excess amount received from *Y* = 300 Shares – 200 Shares
= 100 Shares × ₹8 = ₹800

(B) Amount due from *X* and *Y* on First & Final Call :

		₹
X 300 Shares @ ₹7	=	2,100
Y 200 Shares @ ₹7	=	1,400
		3,500
Less : Excess received on application & allotment from *X* and *Y* (₹800 + ₹800)		1,600
Amount due but not paid on First & Final Call		1,900

(C) Total amount due on First & Final Call

(1,00,000 Shares × ₹7)	= 7,00,000
Less : Excess received on Application & Allotment (Calls in Advance)	= 3,20,000
	3,80,000
Less : Not received from *X* and *Y* on First & Final Call	= 1,900
	3,78,100

ILLUSTRATION 58.

XL Ltd. invited applications for issuing 1,00,000 equity shares of ₹10 each at par. The amount was payable as follows :

On Application ₹3 per share.
On Allotment ₹4 per share.
On First and Final Call ₹3 per share.

The issue was over-subscribed by three times. Applications for 20% shares were rejected and the money refunded. Allotment was made to the remaining applicants as follows.

Category	*No. of Shares Applied*	*No. of Shares Allotted*
I	1,60,000	80,000
II	80,000	20,000

Excess money received with applications was adjusted towards sums due on allotment and first and final call. All calls were made and were duly received except the final call by a shareholder belonging to Category I who has applied for 320 shares. His shares were forfeited. The forfeited shares were re-issued at ₹15 per share fully paid up.

Pass necessary Journal entries for the above transactions in the book of XL Ltd. Open calls in-arrears and calls in advance account whenever required.

(C.B.S.E. 2017, Delhi)

SOLUTION : **Journal of XL Ltd.**

Date	*Particulars*		*L.F.*	*Dr.* (₹)	*Cr.* (₹)
	Bank A/c	Dr.		9,00,000	
	To Share Application A/c				9,00,000
	(Applications received for 3,00,000 shares @ ₹3 each)				
	Share Application A/c	Dr.		9,00,000	
	To Share Capital A/c				3,00,000
	To Share Allotment A/c				3,20,000
	To Calls in Advance A/c				60,000
	To Bank A/c				2,20,000
	(Application money adjusted) (As per Note 1)				
	Share Allotment A/c	Dr.		4,00,000	
	To Share Capital A/c				4,00,000
	(Allotment due on 1,00,000 shares @ ₹4 each)				
	Bank A/c (₹4,00,000 – ₹3,20,000)	Dr.		80,000	
	To Share Allotment A/c				80,000
	(Allotment money received in full)				
	Share First & Final Call A/c	Dr.		3,00,000	
	To Share Capital A/c				3,00,000
	(First & Final Call due on 1,00,000 shares @ ₹3 each)				
	Bank A/c	Dr.		2,39,520	
	Calls in Advance A/c	Dr.		60,000	
	Calls in Arrears A/c	Dr.		480	
	To Share First & Final Call A/c				3,00,000
	(Amount received on First & Final Call) (As per Note 2)				

	Share Capital A/c	Dr.		1,600	
	To Calls in Arrears A/c				480
	To Forfeited Shares A/c				1,120
	(Forfeiture of 160 shares)				
	Bank A/c	Dr.		2,400	
	To Share Capital A/c				1,600
	To Securities Premium A/c				800
	(Reissue of 160 shares @ ₹15 each)				
	Forfeited Shares A/c	Dr.		1,120	
	To Capital Reserve A/c				1,120
	(Transfer of gain on reissue)				

Dr. **CALLS IN ADVANCE ACCOUNT** Cr.

Particulars	*J.F.*	₹	*Particulars*	*J.F.*	₹
To Share First & Final Call A/c		60,000	By Share Application A/c		60,000

Dr. **CALLS IN ARREARS ACCOUNT** Cr.

Particulars	*J.F.*	₹	*Particulars*	*J.F.*	₹
To Share First & Final A/c		480	By Share Capital A/c		480

Working Notes :

(1) In Category (*i*) applicants for 1,60,000 shares are allotted 80,000 shares.

Excess money received on application = 1,60,000 shares – 80,000 shares
= 80,000 shares × ₹3 = ₹2,40,000

Entire excess of ₹2,40,000 will be adjusted on allotment.

In Category (*ii*) applicants for 80,000 shares are allotted 20,000 shares.

Excess money received on application :

		₹
80,000 shares – 20,000 shares = 60,000 shares × ₹3	=	1,80,000
Less : Adjusted on Allotment : 20,000 shares × 4	=	80,000
		1,00,000
Less : Transferred to Calls in Advance A/c : 20,000 shares × ₹3	=	60,000
Amount returned		40,000

Total amount returned :

Returned on 20% applications : 60,000 × ₹3	1,80,000
Returned on Category II applications	40,000
	2,20,000

Total excess application money adjusted on allotment =

Category (*i*)	2,40,000
Category (*ii*)	80,000
	3,20,000

(2) Number of shares applied by Defaulting shareholder = 320

Hence, Shares allotted to him = $320 \times \frac{80,000}{1,60,000} = 160$

Amount not received from Defaulting shareholder on First Call = 160 Shares × ₹3 = ₹480

	₹
Total amount due on First Call : 1,00,000 × ₹3	3,00,000
Less : amount adjusted for Calls in Advance	60,000
	2,40,000
Less : amount not received from defaulting shareholder	480
Net amount received on First Call in Cash	2,39,520

ILLUSTRATION 59.

Bayson Ltd. invited applications for issuing 54,000 shares of ₹100 each payable as follows :

₹50 per share on application

₹10 per share on allotment

Balance on first and final call.

Applications were received for 80,000 shares.

Full allotment was made to the applicants of 14,000 shares. The remaining applicants were allotted 40,000 shares on pro-rata basis. Excess money received with application was adjusted towards sums due on allotment and call.

Vibhor, holding 1,200 shares, who belonged to the category of applicants to whom full allotment was made, paid the call money at the time of allotment. Vidur, who belonged to the category of applicants to whom shares were allotted on pro-rata basis did not pay anything after application on his 400 shares. Vidur's shares were forfeited after the first and final call. All the forfeited shares were later on re-issued at ₹110 per share as fully paid up.

Pass the necessary journal entries in the books of Bayson Ltd. for the above transactions by opening calls in arrears and calls in advance account wherever necessary. *(C.B.S.E. 2017, Comptt.)*

SOLUTION :

Bayson Ltd.

JOURNAL

Date	*Particulars*		*L.F.*	*Dr. Amount*	*Cr. Amount*
				₹	₹
	Bank A/c	Dr.		40,00,000	
	To Equity Share Application A/c				40,00,000
	(Application money received)				
	Equity Share Application A/c	Dr.		40,00,000	
	To Equity Share Capital A/c				27,00,000
	To Equity Share Allotment A/c				4,00,000
	To Calls in Advance A/c (Note 1)				9,00,000
	(Application money transferred)				

	Equity Share Allotment A/c Dr.		5,40,000	
	To Equity Share Capital A/c			5,40,000
	(Share allotment made due on 54,000 shares @ ₹10)			
	Bank A/c Dr.		1,88,000	
	To Equity Share Allotment A/c (Note 2)			1,40,000
	To Calls in Advance A/c (1,200 Shares × ₹40)			48,000
	(Allotment money received alongwith calls in advance on 1,200 shares)			
	Equity Share First & Final Call A/c Dr.		21,60,000	
	To Equity Share Capital A/c			21,60,000
	(First and Final Call due on 54,000 shares @ ₹40)			
	Bank A/c (Note 3) Dr.		12,05,000	
	Calls in Advance A/c (₹9,00,000 + ₹48,000) Dr.		9,48,000	
	Calls in Arrears A/c Dr.		7,000	
	To Equity Share First and Final Call A/c			21,60,000
	(First and Final Call money received)			
	Equity Share Capital A/c Dr.		40,000	
	To Calls in Arrears A/c			7,000
	To Forfeited Shares A/c			33,000
	(400 Shares of Vidur forfeited)			
	Bank A/c Dr.		44,000	
	To Equity Share Capital A/c			40,000
	To Securities Premium Reserve A/c			4,000
	(400 Shares reissued @ ₹110 per share fully paid up)			
	Forfeited Shares A/c Dr.		33,000	
	To Capital Reserve A/c			33,000
	(Gain on reissued shares transferred to Capital Reserve)			

Working Notes :

(1) Applications were received for 80,000 shares and applicants for 14,000 shares were made full allotment. Hence, applicants for 66,000 shares were allotted = 40,000 shares.

		₹
Excess application money received = (66,000 – 40,000) × ₹50	=	13,00,000
Less : Adjusted on Allotment : 40,000 Shares × ₹10	=	4,00,000
Amount transferred to Calls in Advance A/c		9,00,000

	₹
(2) Total Allotment money due	5,40,000
Less : Already received at the time of application	4,00,000
Net amount due on allotment	1,40,000

(3) (*a*) Shares applied by Vidur = $\frac{66,000}{40,000} \times 400$ Shares = 660 Shares ₹

Excess application money received from him = 660 – 400

= 260 Shares × ₹50 = 13,000

	=	4,000
Less : Adjusted on Allotment = 400 Shares × ₹10		
Calls in Advance from Vidur		9,000

(*b*) Amount due from Vidur on First & Final Call = 400 × ₹40	=	16,000
Less : Calls in Advance from Vidur	=	9,000
Amount not paid by Vidur on First and Final Call		7,000

		₹
(*c*) Total Amount due on First & Final Call : 54,000 Shares × ₹40	=	21,60,000
Less : Amount transferred to Calls in Advance (9,00,000 + 48,000)	=	9,48,000
		12,12,000
Less : Not received from Vidur on First and Final Call		7,000
		12,05,000

Utilisation of excess application money for Securities Premium :

ILLUSTRATION 60.

X Ltd. issued for Public subscription 1,00,000 equity shares of ₹10 each at a premium of ₹5 per share payable as under :

On Application	₹5
On Allotment	₹7 (including premium ₹5)
On First & Final Call	₹3

Applications were received for 1,50,000 shares. Allotment was made pro-rata to all the applicants and the money overpaid on application was utilised towards sums due on allotment.

Suruchi, who applied for 1,800 shares failed to pay the allotment and call money and the shares were subsequently forfeited. Two-third of the forfeited shares were re-issued to Supriya as fully paid up at ₹8 per share. Show the journal entries to record the above transactions.

SOLUTION :

***X* Ltd.**

JOURNAL

Date	*Particulars*		*L.F.*	*Dr.* (₹)	*Cr.* (₹)
	Bank A/c	Dr.		7,50,000	
	To Equity Share Application A/c				7,50,000
	(Application money received on 1,50,000 shares @ ₹5 per share)				
	Equity Share Application A/c	Dr.		7,50,000	
	To Equity Share Capital A/c				5,00,000
	To Equity Share Allotment A/c				2,50,000
	(Transfer of application money)				
	Equity Share Allotment A/c	Dr.		7,00,000	
	To Equity Share Capital A/c				2,00,000
	To Securities Premium Reserve A/c				5,00,000
	(Allotment due on 1,00,000 shares @ ₹7 per share)				

	Bank A/c[1]	Dr.		4,44,600	
	Calls in Arrears A/c	Dr.		5,400	
	To Equity Share Allotment A/c				4,50,000
	(Allotment money received except on 1,200 shares of Suruchi)				
	Equity Share First and Final Call A/c	Dr.		3,00,000	
	To Equity Share Capital A/c				3,00,000
	(First & Final call due on 1,00,000 shares @ ₹3 per share)				
	Bank A/c	Dr.		2,96,400	
	Calls in Arrears A/c	Dr.		3,600	
	To Equity Share First and Final Call A/c				3,00,000
	(First & Final call received except on 1,200 shares @ ₹3 per share)				
	Equity Share Capital A/c	Dr.		12,000	
	Securities Premium Reserve A/c[2]	Dr.		5,400	
	To Calls in Arrears A/c				9,000
	To Share Forfeiture A/c				8,400
	(The forfeiture of 1,200 shares)				
	Bank A/c	Dr.		6,400	
	Share Forfeiture A/c	Dr.		1,600	
	To Equity Share Capital A/c				8,000
	(The re-issue of 800 shares at ₹8 per share)				
	Share Forfeiture A/c[3]	Dr.		4,000	
	To Capital Reserve A/c				4,000
	(Gain on reissue transferred to Capital Reserve A/c)				

Working Notes :

(1) (A) Suruchi applied for 1,800 shares. She must have been allotted

$$1,800 \times \frac{1,00,000}{1,50,000} = 1,200 \text{ shares}$$

Excess amount received from Suruchi on Application :

1,800 shares – 1,200 shares = 600 shares × ₹5 = ₹3,000.

		₹
(B)	Amount due from Suruchi on allotment = 1,200 × ₹7	8,400
Less :	Excess amount received on application (Out of this amount, 1,200 × ₹2 = ₹2,400 is part of share capital and balance of ₹600 is a part of securities premium)	3,000
	Amount not paid on allotment	5,400

(C)	Total amount due on allotment : 1,00,000 shares × ₹7	7,00,000
Less :	Excess amount received on application	2,50,000
		4,50,000
Less :	Amount not paid by Suruchi	5,400
	Net amount received on allotment	4,44,600

(2) Securities Premium Reserve related to Suruchi's shares is 1,200 shares × 5 = ₹6,000, out of which ₹600 is already received as excess application money. Hence, balance of ₹5,400 not received will be debited in the entry for forfeiture of her shares.

(3) Calculation of amount transferred to Capital Reserve :

Forfeited amount on 1,200 shares = ₹8,400

Hence, forfeited amount on 800 reissued shares : $\frac{8,400}{1,200} \times 800 =$	5,600
Less : Loss on Reissue : 800 × ₹2	1,600
	4,000

ILLUSTRATION 61.

On 1st Jan. 2022, Saraswati Ltd. issued 50,000 equity shares of ₹10 each at a premium of ₹4 per share, payable as follows :

On Application	₹6	(including ₹1 premium)
On Allotment	₹2	(including ₹1 premium)
On First Call	₹4	(including ₹1 premium)
On Second & Final Call	₹2	(including ₹1 permium)

Applications were received for 65,000 shares, of which applications for 5,000 shares were rejected and their money was refunded. Rest of the applicants were issued shares on pro rata basis and their excess money was adjusted towards allotment.

Ashok, to whom 1,000 shares were allotted, failed to pay the allotment money and his shares were forfeited after allotment. Rohan, who applied for 1,800 shares failed to pay the two calls and his shares were forfeited after the final call.

1,900 forfeited shares were reissued as fully paid on receipt of ₹9 per share, the whole of Rohan's shares being included.

Pass necessary Journal entries.

SOLUTION :

In the Books of Saraswati Ltd.

JOURNAL

Date	*Particulars*	*L.F.*	*Dr. (₹)*	*Cr. (₹)*
	Bank A/c Dr.		3,90,000	
	To Equity Share Application A/c			3,90,000
	(Application money received on 65,000 shares @₹6 per share)			
	Equity Share Application A/c Dr.		3,90,000	
	To Equity Share Capital A/c			2,50,000
	To Securities Premium Reserve A/c			50,000
	To Equity Share Allotment A/c			60,000
	To Bank A/c			30,000
	(Transfer of application money)			
	Equity Share Allotment A/c Dr.		1,00,000	
	To Equity Share Capital A/c			50,000
	To Securities Premium Reserve A/c			50,000
	(Allotment money due on 50,000 shares @₹2 per share)			

Bank A/c(1)	Dr.		39,200	
Calls in Arrears A/c	Dr.		800	
To Equity Share Allotment A/c				40,000
(Allotment money received on 49,000 shares)				
Equity Share Capital A/c (1,000 × ₹6)	Dr.		6,000	
Securities Premium Reserve A/c (Note 4)	Dr.		800	
To Calls in Arrears A/c				800
To Forfeited Shares A/c				6,000
(1,000 shares forfeited due to non-payment of allotment money)				
Equity Share First Call A/c	Dr.		1,96,000	
To Equity Share Capital A/c				1,47,000
To Securities Premium Reserve A/c				49,000
(Amount due on first call on 49,000 shares)				
Bank A/c(2)	Dr.		1,90,000	
Calls in Arrears A/c	Dr.		6,000	
To Equity Share First Call A/c				1,96,000
(First call money received on 47,500 shares)				
Equity Share Second & Final Call A/c	Dr.		98,000	
To Equity Share Capital A/c				49,000
To Securities Premium Reserve A/c				49,000
(Second & Final Call due on 49,000 shares)				
Bank A/c	Dr.		95,000	
Calls in Arrears A/c	Dr.		3,000	
To Equity Share Second & Final Call A/c				98,000
(Second & Final Call received on 47,500 shares)				
Equity Share Capital A/c (1,500 × ₹10)	Dr.		15,000	
Securities Premium Reserve A/c (1,500 × ₹2)	Dr.		3,000	
To Calls in Arrears A/c				9,000
To Forfeited Shares A/c				9,000
(1,500 shares forfeited for non payment of call money)				
Bank A/c (1,900 × ₹9)	Dr.		17,100	
Forfeited Shares A/c (1,900 × ₹1)	Dr.		1,900	
To Equity Share Capital A/c				19,000
(1,900 forfeited shares re-issued)				
Forfeited Shares A/c(3)	Dr.		9,500	
To Capital Reserve A/c				9,500
(Gain on re-issue of shares, transferred to Capital Reserve A/c)				

Working Notes :

(1) (A) Ashok must have applied for $\frac{60,000}{50,000} \times 1,000 = 1,200$ shares.

Excess amount received from Ashok on Application =

1,200 shares – 1,000 shares = 200 shares × ₹6 = ₹1,200

			₹
(B)	Amount due from Ashok on allotment : 1,000 × ₹2	=	2,000
Less :	Excess amount received on application (Out of this amount, 1,000 × ₹1 = ₹1,000 is part of share capital and balance of ₹200 is a part of securities premium)		1,200
	Amount not paid on allotment		800

(C)	Total amount due on allotment : 50,000 shares × ₹2	1,00,000
Less :	Excess amount received on application	60,000
		40,000
Less :	not paid by Ashok	800
	Net amount received on allotment	39,200

(2) Rohan applied for 1,800 shares. He must have been allotted :

$$1{,}800 \times \frac{50{,}000}{60{,}000} = 1{,}500 \text{ shares.}$$

He failed to pay the two calls.
As such, First and Second Call money will be received on
49,000 – 1,500 = 47,500 shares.

(3) 1,900 shares have been reissued which include 1,500 shares of Rohan and 400 shares of Ashok.

Amount forfeited in respect of Rohan's shares	9,000
Amount forfeited in respect of Ashok's shares = $6{,}000 \times \frac{400}{1{,}000}$	2,400
	11,400
Less : Loss on reissue of 1,900 shares @ ₹1 each	1,900
Gain on reissue transferred to Capital Reserve	9,500

(4) Securities Premium Reserve due on allotment on Ashok's shares is 1,000 shares × ₹1 = ₹1,000, out of which ₹200 is already received as excess application money. As such, balance of ₹800 not received by the Company will be debited in the entry for forfeiture of his shares.

ILLUSTRATION 62.

Nickel Ltd. issued Equity shares of ₹10 each at a premium of ₹3 per share payable as ₹4 per share on application, ₹5 per share on allotment (including premium), ₹2 per share on first call and ₹2 per share on final call.

Amit, who had applied for 2,000 shares, was allotted 1,200 shares. He failed to pay the allotment money and on his failure to pay the first call his shares were forfeited.

Out of the forfeited shares, 1,000 were reissued at ₹7 per share.

You are required to pass journal entries for forfeiture and reissue.

(I.S.C. Sample Paper, 2017)

SOLUTION :

JOURNAL

Date	Particulars		L.F.	Dr.	Cr.
				₹	₹
	Share Capital A/c	Dr.		9,600	
	Securities Premium Reserve A/c (₹3,600 – ₹800)	Dr.		2,800	
	To Calls in Arrears A/c(1)				5,200
	To Share Forfeiture A/c				7,200
	(Forfeiture of 1,200 shares)				
	Bank A/c	Dr.		7,000	
	Share Forfeiture A/c	Dr.		1,000	
	To Share Capital A/c				8,000
	(Re-issue of 1,000 shares @ ₹7 per share, ₹8 paid up)				
	Share Forfeiture A/c	Dr.		5,000	
	To Capital Reserve A/c				5,000
	(Transfer to Capital Reserve)				

Working Notes :

		₹
(1) Excess Application money received from Amit :		
2,000 Shares – 1,200 Shares = 800 Shares × ₹4	=	3,200
Amount due from Amit on allotment : 1,200 Shares × ₹5	=	6,000
Less : Excess received from Amit on application (Out of this amount, 1,200 × ₹2 = ₹2,400 is a part of share capital and balance of ₹800 is part of securities premium)		3,200
Amount not paid on allotment		2,800
Amount not paid on 1st Call (1,200 × ₹2)		2,400
Calls in Arrears Amount		5,200

			₹
(2) Amount transferred to Capital Reserve :			
Forfeited amount on 1,200 Shares	=	₹7,200	
∴ Forfeited amount on 1,000 Shares	=	$7{,}200 \times \frac{1{,}000}{1{,}200}$	6,000
Less : Loss on Re-issue			1,000
			5,000

ILLUSTRATION 63.

Khyati Ltd. issued a prospectus inviting applications for 80,000 equity shares of ₹10 each payable as follows :

₹2 on application
₹3 on allotment
₹2 on first call
₹3 on final call

Applications were received for 1,20,000 equity shares. It was decided to adjust the excess amount received on account of over subscription till allotment only. Hence allotment was made as under :

(*i*) To applicants for 20,000 shares — in full
(*ii*) To applicants for 40,000 shares — 10,000 shares
(*iii*) To applicants for 60,000 shares — 50,000 shares

Allotment was made and all shareholders except Tammana, who had applied for 2,400 shares out of the group (*iii*), could not pay allotment money. Her shares were forfeited immediately after allotment. Another shareholder Chhaya, who was allotted 500 shares out of group (*ii*), failed to pay first call. 50% of Tamanna's shares were reissued to Satnaam as ₹7 paid up for payment of ₹9 per share.

Pass necessary journal entries in the books of Khyati Ltd. for the above transactions by opening calls in arrears and calls in advance account wherever necessary. *(C.B.S.E. Sample Paper, 2019)*

SOLUTION :

Books of Khyati Ltd.
JOURNAL

Date	*Particulars*		*L.F.*	*Dr.* (₹)	*Cr.* (₹)
	Bank A/c	Dr.		2,40,000	
	To Equity Share Application A/c				2,40,000
	(Application money received on 1,20,000 shares)				
	Equity Share Application A/c	Dr.		2,40,000	
	To Equity Share Capital A/c				1,60,000
	To Equity Share Allotment A/c(1)				50,000
	To Bank A/c				30,000
	(80,000 shares allotted and excess amount transferred to allotment and refunded)				
	Equity Share Allotment A/c	Dr.		2,40,000	
	To Equity Share Capital A/c				2,40,000
	(Share allotment due on 80,000 shares)				
	Bank A/c(4)	Dr.		1,84,800	
	Calls in Arrears A/c(3)	Dr.		5,200	
	To Share Allotment A/c				1,90,000
	(Allotment money received)				
	Equity Share Capital A/c	Dr.		10,000	
	To Calls in Arrears A/c				5,200
	To Equity Share Forfeited A/c				4,800
	(Forfeiture of 2,000 shares)				
	Equity Share First Call A/c	Dr.		1,56,000	
	To Equity Share Capital A/c				1,56,000
	(Share first call due on 78,000 shares)				
	Bank A/c	Dr.		1,55,000	
	Calls in arrears A/c	Dr.		1,000	
	To Equity Share First Call A/c				1,56,000
	(First call received on 77,500 shares)				

Bank A/c	Dr.		9,000	
To Equity Share Capital A/c				7,000
To Security Premium Reserve A/c				2,000
(1,000 shares reissued as ₹7 paid up, for ₹9 per share)				
Equity Share Forfeited A/c	Dr.		2,400	
To Capital Reserve A/c				2,400
(Gain on reissue of forfeited shares transferred to Capital Reserve)				

Working Notes :

(1) In Category (*ii*) applicants for 40,000 shares are allotted 10,000 shares.
Excess money received on application
= 40,000 shares – 10,000 shares = 30,000 shares × ₹2 = ₹60,000
Since amount due on allotment on these shares is 10,000 shares × ₹3 = ₹30,000 only ₹30,000 out of excess application money of ₹60,000 can be adjusted on allotment and remaining ₹30,000 will be returned.

In Category (*iii*) applicants for 60,000 shares are allotted 50,000 shares.
Excess money received on application
= 60,000 shares – 50,000 shares = 10,000 shares × ₹2 = ₹20,000
Entire excess of ₹20,000 will be adjusted on allotment.
Total excess application money adjusted on allotment =

Category (*ii*)	₹30,000
Category (*iii*)	₹20,000
	₹50,000

(2) Shares allotted to Tammana $= 2{,}400 \times \frac{50{,}000}{60{,}000} = 2{,}000$

Excess application money received from Tammana :
2,400 Shares – 2,000 Shares = 400 Shares × ₹2 = ₹800

(3) Amount due from Tammana on allotment :

	₹
2,000 Shares × ₹3	6,000
Less : Excess received from Tammana on application	800
Amount not received from Tammana on allotment	5,200

(4) Amount received on allotment :

	₹
Total amount due on allotment = 80,000 shares × ₹3	2,40,000
Less : Excess on application money adjusted on allotment	50,000
	1,90,000
Less : Amount not received from Tammana on allotment	5,200
Amount received on allotment in Cash	1,84,800

ILLUSTRATION 64.

Arti Limited invited applications for issuing 80,000 shares of ₹10 each at a premium of ₹4 per share. The amount was payable as follows :

On Application — ₹5 per share
On Allotment — ₹9 per share (Including Premium)

Applications were received for 1,40,000 shares.

Allotment was made on the following basis :

(*i*) To applicants for 80,000 shares — 60,000 shares
(*ii*) To applicants for 60,000 shares — 20,000 shares

Money overpaid on applications was utilized towards sum due on allotment.

Rajiv, who had applied for 1,200 Shares failed to pay his dues and his shares were forfeited.

Pass journal entries in the books of Arti Limited to record the above transactions. *(C.B.S.E. Sample Paper 2010)*

SOLUTION :

Books of Arti Ltd.
JOURNAL

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
	Bank A/c	Dr.		7,00,000	
	To Share Application A/c				7,00,000
	(Application money received on 1,40,000 shares @ ₹5 per share)				
	Share Application A/c	Dr.		7,00,000	
	To Share Capital A/c				4,00,000
	To Share Allotment A/c (Note 1)				2,80,000
	To Bank A/c (Note 1)				20,000
	(Application money adjusted)				
	Share Allotment A/c	Dr.		7,20,000	
	To Share Capital A/c				4,00,000
	To Securities Premium Reserve A/c				3,20,000
	(Allotment money due on 80,000 shares)				
	Bank A/c	Dr.		4,33,400	
	Calls in Arrears A/c	Dr.		6,600	
	To Share Allotment A/c				4,40,000
	(Allotment money received on 79,100 shares)				
	Share Capital A/c	Dr.		9,000	
	Securities Premium Reserve A/c	Dr.		3,600	
	To Calls in Arrears A/c				6,600
	To Share Forfeiture A/c				6,000
	(Forfeiture of 900 shares for non-payment of allotment money)				

Working Notes :

(1) In Category (*i*) applicants for 80,000 shares are allotted 60,000 shares.

Excess money received on application = 80,000 shares – 60,000 shares

= 20,000 shares × ₹5 = ₹1,00,000

Entire excess of ₹1,00,000 will be adjusted on allotment.

In Category (*ii*) applicants for 60,000 shares are allotted 20,000 shares.

Excess money received on application

= 60,000 shares – 20,000 shares = 40,000 shares × ₹5 = ₹2,00,000

Since amount due on allotment on these shares is 20,000 shares × ₹9 = ₹1,80,000, only ₹1,80,000 out of excess application money of ₹2,00,000 can be adjusted on allotment and remaining ₹20,000 will be returned.

Total excess application money adjusted on allotment =

Category (*i*)	₹1,00,000
Category (*ii*)	₹1,80,000
	₹2,80,000

It also shows that defaulter Rajiv belongs to Category (*i*) since full amount of allotment from Category (*ii*) is received on application.

(2) Number of Shares applied by Rajiv = 1,200

Hence, Shares allotted to Rajiv $= 1{,}200 \times \frac{60{,}000}{80{,}000} = 900$

Excess application money received from Rajiv :

1,200 Shares – 900 Shares = 300 Shares × ₹5 = ₹1,500

(3) Amount due from Rajiv on allotment :

	₹
900 Shares × ₹9	8,100
Less : Excess received from Rajiv on application	1,500
Amount not received from Rajiv on allotment	6,600

(4) Amount received on allotment :

		₹
Total amount due on allotment = 80,000 shares × ₹9		7,20,000
Less : Excess received on application		
From Category (*i*)	1,00,000	
From Category (*ii*)	1,80,000	2,80,000
		4,40,000
Less : Amount not received from Rajiv on allotment		6,600
Amount received on allotment in Cash		4,33,400

ILLUSTRATION 65.

ZX Limited invited applications for issuing 5,00,000 Equity shares of ₹10 each at a premium of ₹10 each payable with Final call. Amount per share was payable as follows:

	₹
On Application	2
On Allotment	3
On First Call	2
On Second & Final Call	Balance

Applications for 8,00,000 shares were received. Applications for 50,000 shares were rejected and the application money was refunded. Allotment was made to the remaining applicants as follows :

Category	*Number of Shares Applied*	*Number of Shares Allotted*
I	2,00,000	1,50,000
II	5,50,000	3,50,000

Excess application money received with applications was adjusted towards sums due on allotment. Balance, if any was adjusted towards future calls. Govind, a shareholder belonging to category I, to whom 1,500 shares were allotted paid his entire share money with allotment. Manohar belonging to category II who had applied for 11,000 shares failed to pay 'Second & Final Call money'. Manohar's shares were forfeited after the final call. The forfeited shares were reissued at ₹10 per share as fully paid up.

Assuming that the company maintains "Calls in Advance Account" and "Calls in Arrears Account", pass necessary Journal entries for the above transactions in the books of ZX Limited. *(C.B.S.E. Sample Paper, 2018)*

SOLUTION :

ZX Ltd.

JOURNAL

Date	*Particulars*		*L.F.*	*Dr. Amount*	*Cr. Amount*
				₹	₹
	Bank A/c	Dr.		16,00,000	
	To Equity Share Application A/c				16,00,000
	(Application money received)				
	Equity Share Application A/c	Dr.		16,00,000	
	To Equity Share Capital A/c				10,00,000
	To Equity Share Allotment A/c				5,00,000
	To Bank A/c				1,00,000
	(Application money transferred)				
	Equity Share Allotment A/c	Dr.		15,00,000	
	To Equity Share Capital A/c				15,00,000
	(Allotment money due on 5,00,000 equity shares @ ₹3 each)				
	Bank A/c	Dr.		10,22,500	
	To Equity Share Allotment A/c				10,00,000
	To Calls in Advance A/c (1,500 × ₹15)				22,500
	(Allotment money received alongwith Calls in Advance on 1,500 shares)				
	Equity Share First Call A/c	Dr.		10,00,000	
	To Equity Share Capital A/c				10,00,000
	(First Call money due on 5,00,000 equity shares @ ₹2 each)				
	Bank A/c	Dr.		9,97,000	
	Calls in Advance A/c (1,500 × ₹2)			3,000	
	To Equity Share First Call A/c				10,00,000
	(First call money received)				
	Equity Share Final Call A/c	Dr.		65,00,000	
	To Equity Share Capital A/c				15,00,000
	To Securities Premium Reserve A/c				50,00,000
	(Final Call money due on 5,00,000 equity shares @ ₹13 each including premium of ₹10 each)				

	Bank A/c	Dr.	63,89,500	
	Calls in Advance A/c (1,500 × ₹13)	Dr.	19,500	
	Calls in Arrears A/c(1) (7,000 × ₹13)	Dr.	91,000	
	To Equity Share Final Call A/c			65,00,000
	(Final call money received)			
	Equity Share Capital A/c	Dr.	70,000	
	Securities Premium Reserve A/c	Dr.	70,000	
	To Calls in Arrears A/c			91,000
	To Share Forfeiture A/c			49,000
	(Manohar's Shares forfeited)			
	Bank A/c	Dr.	70,000	
	To Equity Share Capital A/c			70,000
	(7,000 Forfeited Shares re-issued)			
	Share Forfeiture A/c	Dr.	49,000	
	To Capital Reserve A/c			49,000
	(Gain on reissue transferred to Capital Reserve A/c)			

Working Notes :

(1) Shares allotted to Manohar $= \frac{3,50,000}{5,50,000} \times 11,000 = 7,000$

He has not paid Second and Final Call on 7,000 shares.

CASE BASED MCQs — 8

Royal Ltd. invited applications for issuing 2,00,000 equity shares of ₹10 each at a premium of 25% payable with application. Applications for 4,50,000 shares were received. Applications for 1,00,000 shares were rejected and money refunded. Pro-rata allotment was made to the remianing applicants. The amount per share was payable as follows :

On Application	:	₹4 per share including premium
On Allotment	:	₹3.50 per share

Raghu, who had applied for 7,000 shares failed to pay allotment money. His shares were forfeited immediately after allotment. Afterwards the first and final call was made.

Nandan, who had applied for 10,500 shares, failed to pay the first and final call. His shares were also forfeited. Out of the forfeited shares, 7,000 shares were reissued as fully paid up for ₹9 per share including whole of Nandan's shares.

Based on the above information, you are required to answer the following questions :

(*a*) Amount received in cash on allotment will be :

(*i*) ₹1,00,000 (*ii*) ₹6,98,000
(*iii*) ₹ 98,000 (*iv*) ₹ 86,000

(*b*) In the entry of forfeiture of Raghu's shares, amount credited to Share Forfeiture Account will be :

(*i*) ₹28,000 (*ii*) ₹38,000
(*iii*) ₹18,000 (*iv*) ₹12,000

(*c*) Amount credited to Capital Reserve Account will be :

(*i*) ₹26,000 (*ii*) ₹27,500
(*iii*) ₹34,500 (*iv*) ₹41,000

(*d*) Balance in Reserve and Surplus Account will be :

(*i*) ₹5,00,000 (*ii*) ₹ 27,500
(*iii*) ₹5,41,000 (*iv*) ₹5,27,500

(*e*) Subscribed and Fully-paid capital will be :

(*i*) ₹19,70,000 (*ii*) ₹19,83,500
(*iii*) ₹20,00,000 (*iv*) ₹20,13,500

CASE BASED MCQs — 9

X Ltd. invited applications for issuing 2,40,000 equity shares of ₹10 each at a premium of ₹4 per share. The amount was payable as under :

On application	:	₹4 per share (including premium ₹2)
On allotment	:	₹4 per share
On first and final call	:	Balance Amount

Applications for 3,00,000 shares were received and pro-rata allotment was made to all the applicants. All calls were made and were duly received except from Rohini, who failed to pay allotment and first and final call on 7,500 shares applied by her. These shares were forfeited. Afterwards, 40% of the forfeited shares were re-issued at ₹11 per share as fully paid-up.

On the basis of above information, you are required to answer the following questions :

(*a*) Calls in Arrears amount will be :

(*i*) ₹60,000 (*ii*) ₹48,000
(*iii*) ₹54,000 (*iv*) ₹42,000

(*b*) Amount transferred to Capital Reserve will be :

(*i*) ₹7,200 (*ii*) ₹18,000
(*iii*) ₹6,000 (*iv*) ₹ 4,800

(*c*) Balance in Securities Premium Reserve Account will be :

(*i*) ₹9,60,000 (*ii*) ₹9,48,000
(*iii*) ₹9,62,400 (*iv*) ₹9,50,400

(*d*) Balance in Reserve and Surplus Account will be :

(*i*) ₹9,68,400 (*ii*) ₹9,57,600
(*iii*) ₹9,50,400 (*iv*) ₹9,61,200

(*e*) Subscribed and Fully Paid Capital will be :

(*i*) ₹23,64,000 (*ii*) ₹23,40,000
(*iii*) ₹23,74,800 (*iv*) ₹23,50,800

CASE BASED MCQs — 10

EF Ltd. invited applications for issuing 80,000 equity shares of ₹50 each at a premium of 20%. The amount was payable as follows :

On Application : ₹20 per share (including premium ₹5)
On Allotment : ₹15 per share (including premium ₹5)
On First Call : ₹15 per share
On Second and Final Call : Balance amount

Applications for 1,20,000 shares were received. Applications for 20,000 shares were rejected and pro-rata allotment was made to the remaining applicants.

Seema, holding 4,000 shares failed to pay the allotment money. Afterwards, the first call was made. Seema paid allotment money along with the first call. Sahaj who had applied for 2,500 shares failed to pay the first call money. Sahaj's shares were forfeited and subsequently 40% shares were reissued to Geeta for ₹38 per share, ₹40 per share paid up. Final call was not made.

Based on above information, you are required to answer the following questions :

(*a*) Amount received on allotment in Cash will be :

(*i*) ₹11,60,000 (*ii*) ₹8,00,000
(*iii*) ₹ 7,40,000 (*iv*) ₹7,60,000

(*b*) In the entry of forfeiture of Sahaj's shares, amount Credited to Share Forfeiture A/c will be :

(*i*) ₹37,500 (*ii*) ₹50,000
(*iii*) ₹30,000 (*iv*) ₹60,000

(*c*) After the reissue of forfeited shares, amount transferred to Capital Reserve will be :

(*i*) ₹18,400 (*ii*) ₹20,000
(*iii*) ₹10,400 (*iv*) ₹48,400

(*d*) (*i*) Subscribed and fully paid capital will be ₹31,52,000
(*ii*) Subscribed and fully paid capital will be ₹31,82,000
(*iii*) Subscribed but not fully paid capital will be ₹31,82,000
(*iv*) Subscribed but not fully paid capital will be ₹31,52,000

CASE BASED MCQs — 11

V.D. Ltd. invited applications for issuing 2,00,000 equity shares of ₹10 each at a premium of ₹6 per share. The amount per share was payable as follows :

On applications — ₹3 (including premium ₹1)
On allotment — ₹7 (including premium ₹5)
On first and final call — Balance amount

Applications were received for 2,50,000 shares. Application money on 10,000 shares was returned. Shares were alloted to the remaining applicants on pro-rata basis.

The company received all the money due on allotment except from Agam, who was allotted 1,000 shares. Her shares were forfeited immediately after allotment. Afterwards, the first and final call was made. Seema, the holder of 2,000 shares, did not pay the first and final call on her shares. Her shares were also forfeited. 50% of the forfeited shares, each of Agam and Seema, were reissued as fully paid-up @ ₹16 per share.

You are required to answer the following questions :

(*a*) Amount received in Cash on allotment will be :

(*i*) ₹12,80,000 (*ii*) ₹13,93,600
(*iii*) ₹12,73,000 (*iv*) ₹12,73,600

(*b*) In the entry on forfeiture of Agam's shares, amount credited to Share Forfeiture Account will be :

(*i*) ₹2,600 (*ii*) ₹6,400
(*iii*) ₹2,000 (*iv*) ₹8,600

(*c*) After the reissue of forfeited shares, amount credited to Capital Reserve will be :

(*i*) ₹10,600 (*ii*) ₹5,300
(*iii*) ₹ 8,300 (*iv*) ₹7,200

(*d*) Balance in Reserve and Surplus Account will be :

(*i*) ₹12,09,000 (*ii*) ₹ 5,300
(*iii*) ₹12,14,300 (*iv*) ₹12,05,300

(*e*) In the Balance Sheet, Share Forfeiture A/c will be shown under the sub-head:

(*i*) Reserve and Surplus (*ii*) Surplus
(*iii*) Share Capital (*iv*) Other Reserves

(See Answers at the end of the book)

SHORT ANSWER QUESTIONS

(Questions Carrying 2 Marks)

1. What is meant by the term 'Limited liability'?

Ans. The term 'limited liability' is used in the context of joint stock companies. The liability of the members is only limited to the value of shares held by them. When the shares held by them are fully paid up, the members have no further liability. Thus the member is only liable to the extent of amount unpaid on the shares which he holds and can never be called to make any further payment even if the company becomes insolvent at the time of winding up.

2. What are two important documents which are required to be filed for registration of a joint stock company?

Ans. The two important documents to be filed for registration of a company are :

(*i*) Memorandum of association

(*ii*) Articles of Association.

3. Name any two statutory books maintained by the company under Companies Act. *(I.S.C. 2004)*

Ans. (*i*) Register of Members

(*ii*) Register of Investments in shares and debentures of other companies.

4. What is a Cumulative Preference Share?

5. What is a Convertible Preference Share?

6. Write two points of differences between an equity share and a preference share.
7. Define 'Share Capital' of a company. *(I.S.C. 2002)*
8. What is meant by 'Issued capital'?
9. What is meant by 'Subscribed Capital'?
10. Distinguish between Authorised Capital and Issued Capital. *(I.S.C. 2013)*

Ans.

	Authorised Capital		*Issued Capital*
1.	It refers to that amount of Capital which is stated in the Memorandum of Association of the Company as its registered Capital.	1.	It refers to that part of Authorised Capital of the Company which is offered to the public for subscription.
2.	Its amount is determined after considering the present and future requirements.	2.	Its amount is determined after considering the present requirements.
3.	It can exceed issued capital.	3.	It cannot exceed authorised capital.

11. Distinguish between nominal capital and paid up capital. *(I.S.C. 2001)*

Ans. Nominal capital is that amount which is stated in the Memorandum of Association. This is the maximum capital for which a company is authorised to issue shares during its lifetime.

Paid up Capital is the amount actually received in cash from the shareholders. The shareholders are asked by the company to pay on application, allotment and on calls the amount of the shares issued to them and subscribed by them. If the called up amount on the shares subscribed is fully paid up then the paid up capital and called up capital would be the same.

12. Give any two differences between Reserve Capital and Capital Reserve. *(ISC 2016)*

Ans. Differences between Reserve Capital and Capital Reserve.

Basis	*Reserve Capital*	*Capital Reserve*
1. **Creation**	It is created out of uncalled capital.	It is created out of capital profits.
2. **Disclosure**	It is not disclosed in the company's balance sheet.	It is disclosed in the company's balance sheet under Equity and Liabilities, Head-shareholders' Funds, subhead — Reserves and Surplus.
3. **Time when it can be used.**	It can be used only at the time of winding up of the company.	It can be used during the lifetime of the company.

13. Show the Share Capital in Company's balance sheet with imaginary figures.
14. Atleast how much portion of the nominal amount of a share must be called as application money?
15. Explain 'Minimum Subscription'. *(I.S.C. 2004)*

Ans. Section 39 (1) of the Companies Act, 2013 provides that a Company cannot allot any securities of the Company to public unless the amount stated in the prospectus as the minimum amount has been subscribed and the sum payable on application for the amount so stated has been received by the Company by cheque or other instrument which has been paid.

The Companies Act, 2013 has not prescribed the minimum subscription. However, SEBI (Securities and Exchange Board of India) has prescribed that a Company must receive at least 90% of issued share capital before it can proceed with the allotment of shares.

16. What is the maximum amount of a Call according to Table 'F' of Schedule I?

17. What is the minimum time interval between two consecutive calls according to Table 'F' of Schedule I? *(I.S.C. 2005)*

18. 3,000 shares of ₹10 each were issued to the Promoters for their services at a premium of ₹5 per share. Give Journal entry.

19. Apart from issuing shares to the general public for cash, list two other groups to whom a company could issue shares for consideration other than cash. *(ISC Sample Paper, 2017)*

Ans. (*i*) Issue of Shares to Promoters.

(*ii*) Issue of Shares to Underwriters.

(*iii*) Issue of Shares to Vendors.

20. What is meant by public issue of shares?

Ans. When a Company invites the public by issuing a prospectus to subscribe its shares, it is called public issue of shares.

21. State any two uses of Securities Premium as stated in Section 52 of the Companies Act, 2013.

22. Can securities premium be utilised for the purchase of fixed assets? Give reason.

23. Why is 'securities premium on issue' treated as a capital profit in a joint stock company?

Ans. In accordance with the law securities premium on issue of shares is treated as capital profit because it has not been earned in the normal course of business and it is not available for distribution as dividend.

24. When are the shares issued at a premium?

Ans. When the company is fully assured of a high demand for its issue in the market or its existing shares have a high price in the market then it issues its shares at a premium.

25. Can securities premium be freely distributed as dividend?

Ans. No, securities premium cannot be distributed as dividend, as according to the companies Act its use is highly restricted and it permits no deviations.

26. State the provisions of Companies Act 2013 for the issue of shares at a premium.

27. What is meant by Calls-in arrears and Calls-in advance? What is the rate of interest which can be allowed on Calls-in advance and charged on Calls-in arrears?

28. How are Calls-in arrear and Calls-in advance shown in the Balance Sheet?

Ans. Calls-in arrear, though is a debit balance, is not shown on the assets side of Balance Sheet but it is shown by way of deduction from the subscribed but not fully paid capital.

Calls-in advance is shown under 'Current Liabilities', Sub-head 'Other Current Liabilities' in the Company's Balance Sheet.

29. Distinguish between Calls-in arrear and Calls-in advance.

Ans.

Basis	*Calls in Arrears*	*Calls in Advance*
Meaning	Calls-in-Arrears is the amount called up by the company, but not yet paid by the shareholders.	Calls-in-Advance is the amount not yet called up by the company, but paid by the shareholders.
Balance	It shows a debit balance.	It shows a credit balance.
Rate of Interest	As per Table F of Schedule I of the Companies Act, 2013 interest may be charged on calls in arrears at a maximum rate of 10% p.a.	As per Table F of Schedule I of the Companies Act, 2013 interest may be allowed on calls in advance at a maximum rate of 12% p.a.
Income/ Expense	Interest on calls in arrears is an income of the company.	Interest on calls in advance is an expense of the company.

30. Give the adjusting and closing entry for interest on Calls in arrears due from a shareholder. *(I.S.C., 2014)*

Ans. (*i*) Adjusting entry on making due the interest on calls in arrears :

Sundry Members A/c Dr.
To Interest on Calls in Arrears A/c
(Interest charged on Calls in arrears)

(*ii*) Closing entry for interest on Calls in arrears :

Interest on Calls in Arrears A/c Dr.
To Statement of Profit and Loss
(Transfer of interest on Calls in arrears)

31. Distinguish between under-subscription and over-subscription of shares.

Ans.

Basis	*Under-subscription*	*Over-subscription*
Meaning	In case, the number of shares applied for by the public is less than the number of shares offered, it is called under-subscription.	In case, the number of shares applied for by the public is more than the number of shares offered, it is called over-subscription.
Allotment	Full allotment is made to all the applicants in case of under-subscription.	Generally, pro-rata allotment is made to all the applicants in such a case.
Refund	As full allotment is made to all the applicants, there is no excess money to be refunded.	Excess application money is either refunded or adjusted towards allotment and calls.

Minimum Subscription	In this case, a company may face the problem of minimum subscription.	In this case, a company does not face such a problem.

32. What a Company will do when there is over-subscription of shares?

Ans. A Company can allot only that number of shares which it has offered to the public for subscription. Hence, a Company may choose one out of the following three alternatives :

(*i*) **First Alternative :** Rejecting Excess Applications : Excess applications are rejected and full allotment is made to all the remaining applicants.

(*ii*) **Second Alternative :** Pro-rata allotment : All the applicants are allotted shares on proportional basis.

(*iii*) **Third Alternative :** Some applications are accepted in full, some are rejected and others are allotted shares on proportional basis.

33. What a Company will do when there is under-subscription of shares?

Ans. In such a case, the Company can proceed with the allotment of shares applied for, provided the condition of minimum subscription of 90% of the issued amount has been fulfilled.

34. What is forfeiture of shares? When and how the shares of a company can be forfeited?

35. Can fully paid up shares be forfeited? If so, under what circumstances?

(I.S.C. 2000)

Ans. Fully paid-up shares can be forfeited in the following cases :

(*i*) When there is a default in fulfilling any engagement between the members.

(*ii*) When there is expulsion of members, where the articles specifically provide thereof.
[N.C. Sanyal *Vs.* Calcutta Stock Exchange Association Ltd. (1971)].

36. Write journal entries of forfeiture when the shares have been issued (*i*) At par, and (*ii*) At premium.

37. Can forfeited shares be re-issued at a discount? If so, to what extent? Where would you transfer the balance left in the share forfeited account after the re-issue of such shares?

38. What are the conditions on which forfeited shares can be re-issued?

(I.S.C. Specimen Question Paper, 2018)

Ans. The forfeited shares can be re-issued only if the following conditions are fulfilled:

(*a*) The directors must pass a resolution sanctioning the re-issue of forfeited shares.

(*b*) The price charged should not be less than the amount of arrears on the shares forfeited.

39. What is the minimum price at which the forfeited shares can be re-issued? *(I.S.C. 2015, 2018)*

Ans. The forfeited shares can be reissued at any price subject to one condition that, if the re-issue is made at a discount, then the amount of discount must not exceed the amount actually received on such shares at their first issue *i.e.* the amount forfeited.

40. What are the different ways in which the forfeited shares account can be used?

Ans. The credit balance in the Forfeited Shares Account is used to recover the deficiency created when the forfeited shares are re-issued at a discount. Any amount remaining in the Forfeited Shares Account after the re-issue is a Capital Profit and it must be transferred to a Capital Reserve which can be used to write off losses or expenditure of capital nature.

41. Give four examples of capital profits.

Ans. Four examples of capital profits are :

(*a*) Profit on re-issue of forfeited shares
(*b*) Profits earned prior to incorporation.
(*c*) Premium on issue of shares and debentures.
(*d*) Profit on sale or revaluation of fixed assets.

42. What is the main purpose for which a company normally uses its profits?

Ans. A company uses its profits mainly for the purpose of distribution among its shareholders in the form of dividend and bonus shares.

43. State any two purposes for which the securities premium can be utilised? *(I.S.C. 2006)*

Ans. (*i*) For writing off the preliminary expenses of the company, and

(*ii*) For issuing fully paid bonus shares to the shareholders of the company.

44. State two effects of forfeiture of shares. *(I.S.C. 2008)*

Ans. (*i*) Name of the shareholder is removed from the register of members, and

(*ii*) Amount already received on these shares is forfeited by the company.

45. Give any two points of difference (without examples) between tangible and intangible fixed assets. *(ISC Sample Paper 2015)*

Ans.

Basis of Distinction	*Tangible Fixed Assets*	*Intangible Fixed Assets*
(*i*)	These assets have a physical existence *i.e.*, they can be seen and touched.	These assets do not have a physical existence *i.e.*, they cannot be seen and touched.
(*ii*)	These assets are depreciated.	These assets are amortised over a period of time.

46. What are quoted investments? *(ISC 2006)*

Ans. Quoted investments are the investment in shares and debentures of a company which are quoted on a recognised stock exchange. A Company, on payment of prescribed fees and on fulfilment of certain conditions can get its shares and debentures listed on a stock exchange. Only listed investments can be traded through the stock exchange.

As per Schedule III, the aggregate amount of company's quoted and unquoted investments together with their market value should be separately shown in the Balance Sheet.

47. Distinguish between General Reserve and Reserve Fund. *(I.S.C. Specimen Question Paper, 2018)*

Ans. General Reserve : Companies usually do not distribute the entire profits as dividends but keep aside a part of it in the form of General Reserve. Such reserves are also called **'Free Reserves'** because they are not created for any specific purpose and can be freely used for any purpose.

Reserve Fund : When the amount of General Reserve or Specific Reserve instead of being utilised in the business is invested outside the business in securities, it is called 'Reserve Fund'.

48. What is contingent liability? How are contingent liabilities shown in the Balance Sheet of a Company prepared as per Schedule III of the Companies Act 2013? *(ISC 2016)*

Ans. These are the liabilities which may or may not arise because they depend on the happening of some event in the future.

Contingent liability is not recorded in the books of accounts. Hence, it is not shown in the Balance sheet but is disclosed in the 'Notes to Accounts' for the information of the users of financial statements.

49. Give two examples of Contingent Liabilities.

Ans. (*i*) Bills receivable discounted but not matured.

(*ii*) Suit for damages filed against the company by a customer.

50. What is meant by 'Current Maturities of Long Term Debt'? How is it disclosed in the Balance sheet of a company? *(ISC Sample Paper, 2017)*

Ans. Amount due to be paid within 12 months of the date of Balance Sheet or within the period of operating cycle out of long-term borrowings is known as current maturities of long term debts.

For example, *X* Ltd. issues ₹10,00,000 debentures on 1st April, 2016 redeemable in five equal yearly instalments starting from 1st April, 2017. In this case ₹2,00,000 redeemable within 12 months from the date of Balance Sheet *i.e.*, as at 31st March, 2017 will be shown as 'Current Maturity of Long-term Debts' and balance ₹8,00,000 will be shown as Long-term Borrowings.

Current Maturities of Long-term Debt is shown under Main bead 'Current Liabilities' and sub-head 'Other Current Liabilities' in the Balance Sheet of the Company.

51. State, with reason, whether securities premium reserve can be used to write off bad debts. *(I.S.C. 2017)*

OR

State with reason whether Securities Premium Reserve can be used by a company to write off the discount allowed to its debtors. *(I.S.C. 2020)*

Ans. 'Securities Premium Reserve' cannot be used either to write off bad debts or to write off the discount allowed to its debtors. It is a capital profit and can be used only for those purposes which are specified under section 52 of Companies Act, 2013. Discount allowed to debtors is a revenue expense and charge against profits.

52. State where will the non-cash transactions be recorded at the time of issue of shares, if all cash transactions are entered in the Cash Book. *(I.S.C. 2017)*

Ans. Non-Cash transactions will be recorded in Journal/Journal Proper.

OBJECTIVE TYPE QUESTIONS

Choosing out of the words provided, fill in the blanks given below :

(*i*) Equity shareholders are .... of the Company *(Creditors, Owners, Customers)*

(*ii*) Preference shareholders are .... of the Company. *(Creditors, Owners, Customers)*

(*iii*) Premium received on the issue of shares is shown on the .... side of the Balance Sheet. *(Assets, Equity & Liabilities)*

(*iv*) The liability of every shareholder of a Company is .... *(Limited, Unlimited)*

(*v*) Share Application is a .... account. *(Personal, Real, Nominal)*

(*vi*) Minimum Share Application money is ....% of the nominal value of shares. *(5, 20, 25)*

(*vii*) There must be an interval of atleast .... month between the making of the two calls. *(One, three)*

(*viii*) According to Table 'F' of Schedule I interest on calls in advance may be paid at a rate not exceeding .... % p.a. *(10, 12)*

(*ix*) Shareholders get .... *(Interest, Dividend)*

Ans. (*i*) Owners; (*ii*) Owners; (*iii*) Equity and Liabilities; (*iv*) Limited; (*v*) Personal; (*vi*) 25; (*vii*) One; (*viii*) 12; (*ix*) Dividend.

PRACTICAL QUESTIONS

(Question No. 1 to 62 are strictly in the serial order of Illustrations)

Issue of Shares at Par

Q. 1. Vikas Ltd. has an authorised capital of ₹40,00,000 divided into 4,00,000 Equity Shares of ₹10 each. Out of these, the company invited applications for 3,00,000 equity shares.

The public applied for 2,80,000 shares and all the money was duly received.

Show how Share Capital will appear in the Balance Sheet of the Company. Also prepare notes to accounts.

[Ans. Subscribed and Fully Paid Capital ₹28,00,000]

Q. 2. 'Tractors India Ltd.' is registered with an authorised capital of ₹10,00,000 divided into 1,00,000 equity shares of ₹10 each. The company issued 50,000 equity shares at a premium of ₹5 per share. ₹2 per share were payable with application, ₹8 per share including premium on allotment and the balance amount on first and final call. The issue was fully subscribed and all the amount due was received except the first and final call money on 500 shares allotted to Balram.

Present the 'Share Capital' in the Balance Sheet of 'Tractors India Ltd.' as per Schedule III Part I of the Companies Act, 2013, Also prepare Notes to Accounts for the same.

[Ans.	Subscribed and Fully Paid Capital	₹4,95,000
	Subscribed but Not Fully Paid Capital	₹ 2,500]

Q. 3. Nupur Ltd. was registered with an Authorised Capital of ₹20,00,000 divided into 2,00,000 equity shares of ₹10 each. The Company offered 1,50,000 equity shares for subscription to public and applications were received for 1,40,000 equity shares. The directors called ₹7 per share upto 31st March and the money called was duly received.

Show the Share Capital in the Balance Sheet of the Company together with notes to accounts.

[Ans. Subscribed but not fully paid capital ₹9,80,000.]

Q. 4. Rama Co. issued 50,000 shares of ₹10 each payable as follows :

₹3 on Application;	₹3 on Allotment
₹2 on First Call;	₹2 on Final Call.

All the shares were subscribed and allotted. Give Journal entries and show how the Share Capital will appear in the Balance Sheet assuming that all sums have been duly received. Expenses on issue of shares amounted to ₹10,000.

Issue of Shares at Premium

Q. 5. *Z* Ltd. was registered with an authorised capital of ₹60,00,000 divided in 60,000 equity shares of ₹100 each. Company issued 25,000 equity shares at a premium of ₹20 per share, payable as follows : ₹30 on Application; ₹45 on Allotment (including premium); ₹20 on first call and ₹25 on Second and Final Call.

All shares were subscribed and all the money was duly received. Share issue expenses amounted to ₹40,000 which were fully written off against Securities Premium.

Prepare necessary Journal Entries, Bank Account and Opening Balance Sheet.

[Ans. Share Capital ₹25,00,000; Reserve and Surplus ₹4,60,000; Balance at Bank ₹29,60,000.]

Q. 6. Kanpur Gas Ltd. issued 40,000 equity shares of ₹10 each at a premium of ₹1 per share. Amounts were payable as follows :

₹2.50 on Application; ₹4.50 on Allotment (including premium); ₹2 on First Call and ₹2 on Final Call.

Applications were received for 37,000 shares.

Give Journal Entries and Balance Sheet assuming that all sums have been received on due dates.

[**Ans.** Share Capital ₹3,70,000; Reserve & Surplus ₹37,000; Cash at Bank ₹4,07,000.]

Shares issued for consideration other than cash

Q. 7. Bhawna Ltd. was registered with a nominal capital of ₹1,00,000 divided into shares of ₹10 each. The company purchased assets for ₹27,000 from Bhatia-Singhal. The company issued fully paid equity shares of ₹10 each in satisfaction of the claim. Shares of ₹10,000 were issued at par to the promoters for their services.

Give journal entries of the above transactions if Bhatia-Singhal were issued shares at (*i*) par; and (*ii*) 20% premium.

[**Ans.** Face value of shares issued in case (*i*) ₹27,000; and Case (*ii*) ₹22,500.]

Q. 8. Pass journal entries for the following :

(*i*) *X* Ltd. purchased Land and Building from *R*. Sundram for ₹5,00,000 payable in fully paid shares of ₹100 each at a premium of 25%.

(*ii*) *Y* Ltd. decided to issue 2,000 shares of ₹100 each to the Unit Trust of India as Underwriting Commission.

[**Ans.** (*i*) 4,000 shares of ₹100 each issued at ₹25 per share premium]

Q. 9. Tagore Ltd. purchased a running business from Tulsi Bros. for a sum of ₹48,00,000 payable by the issue of fully paid equity shares of ₹20 each at a premium of 20%. The assets and liabilities consisted of the following :

	₹
Plant and Machinery	25,00,000
Stock	15,00,000
Sundry Debtors	8,60,000
Sundry Creditors	3,00,000

Pass the necessary journal entries in the books of Tagore Ltd.

[**Ans.** Goodwill ₹2,40,000; Number of shares issued 2,00,000. Premium on Issue of shares ₹8,00,000.]

Q. 10. Madhur Ltd. took over the assets of ₹3,90,000 and Liabilities of ₹40,000 of Rasova Ltd. for a consideration of ₹4,00,000. 20% was paid by a cheque and the balance by issue of fully paid equity shares of ₹100 each at a premium of 60%. Show necessary journal entries for these transactions in the books of Madhur Ltd.

[**Ans.** Goodwill ₹50,000; Number of shares issued 2,000.]

Calls in Arrear

Q. 11. *X* Ltd. issued 20,000, 7% Preference shares of ₹100 each at a premium of 6%. Payments were to be made as — ₹25 on Application; ₹46 on Allotment, ₹10 on First call and ₹25 on Final Call.

The applications for 18,000 shares were received and all were accepted. All the money was duly received except the first and final call on 100 shares.

Give the necessary Journal Entries and prepare Cash Book of the Company. Also give the Opening Balance Sheet of the Company.

[**Ans.** First Call in arrear ₹1,000; Final Call in arrear ₹2,500; Share Capital ₹17,96,500; Securities Premium Reserve ₹1,08,000; Cash at Bank ₹19,04,500.]

Hint : It will be assumed that premium is included in allotment.

Q. 12. Vishal Ltd. issued 50,000 Equity Shares of ₹10 each payable as follows :

₹2 on application	payable on 1st June 2020
₹3 on allotment	payable on 1st August 2020
₹3 on first call	payable on 1st Nov. 2020
Balance on final call	payable on 1st Jan. 2021.

All the shares were subscribed except the following :

(*i*) Shareholder Suresh, holding 1,000 shares did not pay the first call and final call.

(*ii*) Shareholder Vasudev, holding 2,000 shares did not pay the final call.

These amounts were due till the date of Balance Sheet on 31st March, 2021. Articles of Association of the Company provided for charging interest on calls in arrears @10% p.a.

Pass necessary journal entries and show Share Capital in the Balance Sheet of the company.

Ans. (*i*) Entry for interest due on calls in Arrears :

	Dr.	Cr.
Sundry Members A/c	Dr. 275	
To Interest on Calls in Arrears A/c		275

(*ii*) Presentation of Share Capital in the Balance Sheet :

	₹
Issued Capital	5,00,000
Subscribed and Fully Paid Capital	4,70,000
Subscribed but not Fully Paid Capital	21,000

Calls in Advance

Q. 13. Aman Ltd., issued 40,000 shares of ₹10 each to the public and received the amount as :

On 1.3.2021 with application ₹2.50; on allotment ₹2.50 on 1.7.2021; on first call ₹3 on 1.12.2021 and the balance amount on final call on 1.3.2022. Ramesh, who had 500 shares, paid the amount of first and final call with allotment and Mohan, who had 100 shares paid the amount of final call with first call. According to Articles of Association interest on call in advance is to be paid @ 12% p.a. The interest was paid on 1.3.2022. Give Journal entries in the books of the Company assuming that books are closed on 31st March every year.

[**Ans.** Interest on Calls in Advance ₹161.]

Q. 14. Chandra Ltd. issued 40,000 equity shares of ₹10 each at par payable as to: ₹2.50 on application; ₹2.00 on allotment; ₹2.50 on first call and ₹3.00 on final call (Three months after First Call).

All the shares were allotted and amount received except Mohan holding 800 shares paid the final call money alongwith first call and Naresh holding 300 shares did not pay the first call money in time.

Final call was made. All the shareholders paid in full. First call arrear on 300 shares alongwith interest on calls in arrears were also received at the time of final call. The company paid interest on calls in advance and charged interest on calls in arrears according to the provisions of Table F of schedule I of Companies Act, 2013.

Make entries in the company's journal for transactions relating to first call and final call.

[**Ans.** Amount received on First Call ₹1,01,650 (₹1,00,000 – ₹750 + ₹2,400); Interest on Calls in Advance ₹72; Interest on Calls in Arrears ₹18.75 or ₹19.]

Q. 15. A limited Company was registered with a capital of ₹5,00,000 in shares of ₹10 each and issued 20,000 such shares at a premium of ₹2 per share, payable as ₹3 per share on application, ₹4 per share on allotment (including premium) and ₹2 per share on first call made three months later. All the money payable on application and allotment were duly received but when the first call was made, one shareholder paid the entire balance on his holdings of 300 shares, and another shareholder holding 1,000 shares failed to pay the first call money.

Give Journal entries to record the above transactions and show how they will appear in the company's Balance Sheet.

[**Ans.** Cash at Bank ₹1,78,900; Amount received on first call ₹38,900 (₹40,000 – ₹2,000 + ₹900).]

Hint : Second Call has not been made in the question, as such, the entries are to be passed upto first call only.

Q. 16. Kaveri Ltd., with an authorised capital of 3,00,000 equity shares of ₹10 each, of which 1,50,000 have already been issued, issues a prospectus offering 1,00,000 shares at a premium of ₹2 per share payable as follows :

On Application	₹5 (including premium)
On Allotment	₹3
On First Call	₹2
On Second & Final Call	₹2

The issue was oversubscribed and money relating to 12,000 applicants was returned.

All calls were made.
Allotment money was not received on 1,000 shares;
First Call money was not received on 1,500 shares;
Second and Final Call money was not received on 2,200 shares.
Share issue expenses amounted to ₹20,000.

You are required to :

(*i*) Record the foregoing transactions of Kaveri Ltd. by way of Ledger Accounts;
(*ii*) Show the relevant items in the Balance Sheet.

[**Ans.** Share Capital ₹24,89,600 (25,00,000 *less* Calls-in-arrears ₹10,400); Security Premium Reserve ₹1,80,000 (after writing off share issue exp.); Cash at Bank ₹11,69,600.]

Over-Subscription

Q. 17. Jupiter Ltd. issued 50,000 shares of ₹10 each payable as follows :

₹2.50 on Application	payable on 1st June, 2021
₹2.50 on Allotment	payable on 1st Aug., 2021
₹2.00 on Ist Call	payable on 1st Dec., 2021
₹3.00 on IInd & Final Call	payable on 1st March, 2022

Applications were received for 1,00,000 shares and the allotments were made as under :

Number of Shares Applied	*Number of Shares Allotted*
42,000	42,000
30,000	8,000
28,000	Nil

Excess money received on application was utilised towards allotment and subsequent calls. Interest on Calls in advance was paid @ 12% p.a.

Give journal entries, assuming all sums due were received and the company closes its books on 31st March every year.

[**Ans.** Amount received on allotment ₹1,05,000; on first call ₹84,000 and on second and final call ₹1,31,000. Interest on Calls in Advance ₹1,970.]

Hint : Interest is allowed on that amount which is transferred to Calls in Advance A/c.

Q. 18. On October 1, 2021, *X* Ltd. offered 1,00,000 shares of ₹10 each payable as follows :

On Application	₹3 per share
On Allotment (November 1, 2021)	₹2 per share
On First Call (December 1, 2021)	₹3 per share
On Second and Final Call (One month after first call)	₹2 per share

Applications were received for 1,25,000 shares on October 15, 2021. Applications for 1,20,000 shares were allotted 1,00,000 shares and the remaining applications were rejected.

Give journal entries assuming that all amounts have been received and the company maintains a combined account of application and allotment.

Forfeiture of Shares Issued at Par

Q. 19. *X* Ltd. was registered with an authorised capital of 2,00,000 shares of ₹10 each. It purchased assets of *Y* Ltd. for ₹3,00,000 and issued fully paid shares for purchase consideration. It also invited applications for 1,20,000 shares payable as under :

₹2.50 on application
₹2.50 on allotment
₹2 on first call and ₹3 on final call.

Amount due on Allotment and First Call was duly received. However, ₹3,58,800 were received on final call. Directors forfeited the shares of defaulting shareholders and reissued them at ₹8.50 per share as fully paid up. Pass entries in the Cash Book and Journal. Also prepare the opening Balance Sheet of the Company.

[**Ans.** Cash at Bank ₹12,02,200; Capital Reserve ₹2,200; Total of Balance Sheet ₹15,02,200.]

Hint. Shares forfeited 400.

Q. 20. Alfa Ltd. issued 5,000 shares of ₹100 each at par. The amount payable was as under :

₹25 on application;
₹25 on allotment;
₹20 on first call; and
₹30 on final call.

The company did not make final call. *X*, a holder of 100 shares, failed to pay allotment and first call money. Directors forfeited his shares and immediately re-issued the forfeited shares at ₹6,500.

Pass Journal entries in the books of the company and prepare the Opening Balance Sheet.

[**Ans.** Cash at Bank ₹3,52,000; Share Capital ₹3,50,000; Capital Reserve ₹2,000.]

Q. 21. Dinesh Ltd. issued 5,000 shares of ₹100 each at par, payable as follows :

	₹
On Application	25
On Allotment	25
On First Call	20
On Final Call	30

Anil, holding 100 shares failed to pay the amount of allotment and first call and his shares were forfeited after the first call.

Sunil, holding 200 shares failed to pay the amount due on final call and his shares were also forfeited.

Show entries in the Cash Book and Journal of the Company and also prepare the Balance Sheet.

[**Ans.** Cash at Bank ₹4,86,500; Balance of Share Forfeiture Account ₹16,500; Total of Balance Sheet ₹4,86,500.]

Q. 22. Fast Food Ltd. issued a prospectus offering 10,000 equity shares of ₹50 each at par payable as follows :

	₹
On Application	15
On Allotment	10
On First Call	15
On Final Call	10

Ram, the holder of 500 equity shares did not pay the amount due on both the calls. These 500 shares were forfeited by the Board of Directors and 300 of these shares were subsequently re-issued at ₹55 per share.

Show the entries in the Cash Book and Journal of the Company. Also prepare the Opening Balance Sheet.

[**Ans.** Cash at bank ₹5,04,000; Share Capital ₹4,90,000; Balance left in Share Forfeiture A/c ₹5,000; Capital Reserve ₹7,500; Securities Premium ₹1,500.]

Q. 23. On 1st April, 2021 Kanishk Ltd. made an issue of 4,000 Equity shares of ₹100 each, payable as follows :

	₹
On Application	30
On Allotment	20
On 1st Call	40
On 2nd and Final Call	10

Applications were received for 10,000 shares and pro-rata allotment was made to all the applicants.

Excess money received on application was utilised towards allotment and subsequent calls. One shareholder who had applied for 500 shares did not pay the final call and his shares were forfeited. Of the forfeited shares, the company reissued 150 shares as fully paid up at ₹90 per share.

You are required to pass journal entries in the books of the company for the year ending 31st March, 2022.

[**Ans.** Amount transferred to Calls-in-advance ₹1,00,000; Amount received on 1st call ₹60,000; Transfer to Capital Reserve ₹12,000.]

Hint. Since all amount due on allotment has already been received on application, there would be no entry for receipt of allotment money.

Q. 24. *W* Ltd. issued 10,000 shares of ₹100 each. During the year only ₹80 were called payable as follows :

On Application	₹25
On Allotment	₹20
On Ist Call	₹20
On IInd Call	₹15

Amounts were received as follows :

On 8,000 shares the full amount called
On 1,200 shares ₹65 per share
On 500 shares ₹45 per share
On 300 shares ₹25 per share

The directors forfeited those shares on which less than ₹65 per share were received. Show entries in the Cash Book and Journal and prepare the Balance Sheet.

[**Ans.** Cash at Bank ₹7,48,000; Amount received on Allotment ₹1,94,000; On First Call ₹1,84,000 and on Second Call ₹1,20,000; Balance of Share Forfeiture Account ₹30,000; Calls in arrears ₹18,000; Balance Sheet Total ₹7,48,000.]

Q. 25. 'Suvidha Ltd.' is registered with an authorized capital of ₹10,00,00,000 divided into 10,00,000 equity shares of ₹100 each. The company issued 1,00,000 shares for public subscription. A shareholder holding 100 shares, failed to pay the final call of ₹20 per share. His shares were forfeited. The forfeited shares were re-issued at ₹90 per share as fully paid up.

Present the 'Share Capital' in the Balance Sheet of the company as per Schedule III Part I of the Companies Act, 2013. Also prepare 'Notes to Accounts'.

[**Ans.** Subscribed and Fully Paid Capital ₹1,00,00,000]

Q. 16 On 1st April, 2021, Blue Heaven Ltd. was formed with an authorised capital of ₹20,00,000 divided into 2,00,000 equity shares of ₹10 each. The company issued prospectus inviting applications for 1,50,000 equity shares. The company received applications for 1,40,000 equity shares. During the first year, ₹7 per share were called. Arun holding 4,000 shares and Varun holding 3,000 shares did not pay the first call of ₹2 per share. Varun's shares were forfeited after the first call and later on 1,800 of the forfeited shares were re-issued at ₹5 per share, ₹7 called up.

Show the following :

(*a*) Share Capital in the Balance Sheet of the company as per Schedule III Part I of the Companies Act, 2013.

(*b*) Also prepare 'Notes to Accounts' for the same.

[*Ans.* Subscribed but not fully paid capital ₹9,69,600.]

Q. 17. *A*, who holds 200 shares of ₹100 each, has paid only ₹25 per share as application money.

B, who holds 300 shares of ₹100 each, has paid ₹25 per share on application and ₹30 per share on allotment.

C, who holds 400 shares of ₹100 each, has paid ₹25 per share on application, ₹30 per share on allotment and ₹20 per share on first call.

They failed to pay their arrears and the final call. Their shares were forfeited and re-issued at ₹95 per share.

Prepare necessary journal entries.

[*Ans.* Capital Reserve ₹47,000.]

Q. [illegible] Pass journal entries for the forfeiture and re-issue in the following cases :

(*i*) *A* Ltd. forfeited 100 shares of ₹10 each fully called-up for non-payment of first call of ₹3 per share and final call of ₹3 per share. All of these shares were re-issued as fully paid for ₹10 per share.

(*ii*) *B* Ltd. forfeited 400 shares of ₹10 each fully called-up for non-payment of final call of ₹3 per share. 300 of these shares were re-issued as fully paid for ₹8 per share.

(*iii*) *C* Ltd. forfeited 700 shares of ₹10 each fully called-up on which the holder has paid application money @ ₹3 and allotment money @ ₹2 per share. Out of these, 300 shares were re-issued as fully paid @ ₹7 per share.

(*iv*) *D* Ltd. forfeited 1,000 shares of ₹10 each fully called-up on which the holder has paid only the application money @ ₹3 per share. Out of these, 600 shares were re-issued at ₹10.50 per share, fully paid up.

[*Ans.* Amount transferred to Capital Reserve : Case (*i*) ₹400; Case (*ii*) ₹1,500; Case (*iii*) ₹600; Case (*iv*) ₹1,800.]

Q. [illegible] Pass journal entries for the forfeiture and re-issue in the following cases :

(*a*) *X* Ltd. forfeited 700 shares of Ashok of ₹10 each ₹8 called-up, on which he had paid ₹5 per share. Out of these, 500 shares were re-issued for ₹9 per share as fully paid.

(*b*) *Y* Ltd. forfeited 400 shares of ₹10 each, ₹6 called-up, for non-payment of first call of ₹2 per share. Out of these, 300 shares were immediately re-issued at ₹5 per share.

(*c*) *Z* Ltd. forfeited 300 shares of ₹100 each on which first call of ₹20 per share was not received, the second and final call of ₹30 per share has not yet been called. Out of these, 200 shares were re-issued as ₹70 paid-up for ₹55 per share.

[**Ans.** Capital Reserve (*a*) ₹2,000; (*b*) ₹900; (*c*) ₹7,000.]

Q. 30. Journalise the following :

(*i*) *A* Ltd. forfeited 1,000 shares of ₹10 each, ₹8 paid, for non-payment of final call of ₹2 per share. Out of these, 400 shares were re-issued as fully paid-up in such a way that ₹2,000 were transferred to capital reserve.

(*ii*) *B* Ltd. forfeited 1,000 shares of ₹10 each, ₹8 called-up, for non-payment of Allotment of ₹2.50 per share and first call of ₹3 per share. Out of these, 400 shares were re-issued for ₹7 per share as ₹8 paid-up.

(*iii*) *C* Ltd. forfeited 300 shares of ₹10 each on which ₹7 has been called and ₹5 has been paid. Out of these, 100 shares are re-issued for ₹6 per share as ₹7 paid-up.

[**Ans.** (*i*) Reissue price ₹7 per share; Capital Reserve (*ii*) ₹600; (*iii*) ₹400.]

Forfeiture of Shares Issued at Premium

Q. 31. *X* Ltd. issued a prospectus offering 2,00,000 shares of ₹10 each at ₹14 per share, payable as follows :

On Application	₹4
On Allotment	₹6 (including premium ₹4)
On First Call	₹3
On Final Call	Balance

Dinesh, the holder of 1,000 shares, did not pay the amount due on allotment and first call. His shares were forfeited and 400 of these shares were immediately re-issued credited ₹9 paid for ₹8.40 per share.

Final call was made afterwards and it was duly received.

Show entries in the Cash Book and the Journal of the company. Also prepare the Opening Balance Sheet.

[**Ans.** Cash at Bank ₹27,93,760; Balance of Share Forfeiture A/c ₹2,400; Capital Reserve ₹1,360; Balance of Securities Premium Reserve A/c ₹7,96,000; Total of Balance Sheet ₹ 27,93,760.]

Q. 32. Vikram Ltd. issued 50,000 shares of ₹10 each at a premium of ₹1 per share payable as follows :

₹3 on Application
₹4 on Allotment (including premium)
₹2 on Ist Call
Balance when required

Applications were received for 46,000 shares and all of these were accepted. Directors did not make the final call. A shareholder holding 800 shares did not pay the amount due on first call. The shares were forfeited and re-issued at ₹7 per share, ₹8 per share paid.

Pass Cash Book and Journal Entries.

[**Ans.** Cash at Bank ₹4,18,000; Capital Reserve ₹4,000.]

Q. 33. *X* Ltd. invited applications for 5,00,000 equity shares of ₹10 each at a premium of 10% payable as under :

On Application ₹3; On Allotment ₹3; On First Call ₹2; and On Final Call ₹2.

Applications were received for 4,50,000 shares and all of these were accepted. The whole of the issue was called for by the company and all the money were duly received except the calls money on 500 shares. These shares were, therefore, forfeited and 300 of these shares were re-issued at ₹8 per share as fully paid. Pass the necessary journal entries to record the above transactions and prepare the Balance Sheet of the Company.

[**Ans.** Cash at Bank ₹49,50,400; Capital Reserve ₹1,200; Securities Premium Reserve ₹4,50,000; Balance of Share Forfeiture Account ₹1,200; Total of Balance Sheet ₹49,50,400.]

Hint : Amount due on allotment will be ₹4 (including premium).

Q. 34. Give journal entries for forfeiture and re-issue of shares :

(*a*) *X* Ltd. forfeited 500 shares of ₹100 each, ₹75 called-up, issued at 10% premium (to be paid at the time of allotment) for non-payment of a first call of ₹20 per share. Out of these, 200 shares were re-issued as ₹75 paid-up for ₹60 per share.

(*b*) *X* Ltd. forfeited 300 shares of ₹100 each, ₹75 called-up, issued at 10% premium (to be paid at the time of allotment) for non-payment of allotment money of ₹30 per share (including premium) and first call of ₹20 per share. Out of these, 100 shares were re-issued as fully paid-up in such a way that ₹3,100 were transferred to Capital Reserve.

[**Ans.** (*a*) Capital Reserve ₹8,000; (*b*) Reissue Price ₹96 per share]

Q. 35. Journalise the following :

(*a*) *Y* Ltd. forfeited 400 shares of ₹100 each, issued at a premium of ₹5 per share (to be paid at the time of allotment) for non-payment of a first call of ₹20 per share. The second and final call of ₹20 has not yet been called. Out of these, 100 shares were re-issued on fully paid-up for ₹110 per share.

(*b*) *Y* Ltd. forfeited 700 shares of ₹100 each, issued at a premium of ₹5 per share for non-payment of allotment money of ₹35 per share (including premium) and first call of ₹20 per share. The second and final call of ₹20 has not yet been called. 500 of these shares were re-issued as ₹80 paid-up for ₹92 per share.

[**Ans.** Capital Reserve (*a*) ₹6,000; (*b*) ₹15,000.]

Q. 36. *A* Co. Ltd. offered to the public 20,000 equity shares of ₹100 each at a premium of ₹10 per share. The payment was to be as follows :

On Application	₹30 per share
On Allotment	₹30 per share (including premium)
On First Call	₹25 per share
On Second & Final Call	₹25 per share

Applications were received for 35,000 shares. Applications for 10,000 shares were rejected. Applicants for 15,000 shares were allotted 10,000 shares and remaining applications were accepted in full. The Directors made both the calls. One shareholder holding 500 shares failed to pay the two calls and as a consequence his shares were forfeited. 200 of these shares were re-issued as fully paid at ₹80 per share.

Expenses of issue came to ₹10,000.

Prepare Cash Book, the Journal and the Balance Sheet on the basis of information given above.

[**Ans.** Cash at Bank ₹21,81,000; Balance of Securities Premium Reserve A/c ₹1,90,000; Balance of Share Forfeiture A/c ₹15,000; Capital Reserve ₹6,000; Total of Balance Sheet ₹21,81,000.]

Hint : Expenses of issue have been written off against Securities Premium A/c.

Q. 37. Elite Ltd. invited applications from public for 5,00,000 equity shares of ₹10 each issued at ₹11 per share. The payment was to be made as follows : ₹3 on Application; ₹4 on Allotment including premium, and ₹4 on call.

Applications for 6,50,000 shares were received. Allotment of shares was made as follows : (*i*) 100% shares to applicants of 4,00,000 shares; (*ii*) 50% shares to applicants of 2,00,000 shares, (*iii*) No allotment to applicants of 50,000 shares.

A shareholder to whom 500 shares were allotted under category (*i*) paid full amount due on shares along with allotment money. Another shareholder holding 1,000 shares failed to pay the amount due on call. His shares were forfeited and 800 of these shares were subsequently re-issued as fully paid-up @ ₹8 per share.

Pass the journal entries and give Balance Sheet of the company.

[**Ans.** Cash at Bank ₹55,02,400; Balance of Securities Premium Reserve A/c ₹5,00,000; Balance of Share forfeiture A/c ₹1,200; Capital Reserve ₹3,200; Balance Sheet total ₹55,02,400.]

Q. 38. AXN Ltd. invited applications for issuing 1,00,000 equity shares of ₹10 each at a premium of ₹6 per share. The amount was payable as follows :

On Application	₹4 per share (including ₹2 premium)
On Allotment	₹5 per share (including ₹2 premium)
On First Call	₹4 per share (including ₹2 premium)
On Second and Final Call	Balance Amount.

The issue was fully subscribed.

Kumar, the holder of 400 shares did not pay the allotment money and Ravi the holder of 1,000 shares paid his entire share money alongwith allotment money. Kumar's shares were forfeited immediately after allotment. Afterwards first call was made. Gupta, a holder of 300 shares failed to pay the first call money and Gopal a holder of 600 shares paid the second call money also alongwith first call. Gupta's shares were forfeited immediately after the first call. Second and final call was made afterwards. The whole amount due on second call was received.

All the forfeited shares were re-issued at ₹9 per share fully paid up.

Pass necessary Journal Entries for the above transactions in the books of the company. *(C.B.S.E. 2017, Delhi)*

[**Ans.** Forfeited amount in respect of Kumar's shares ₹800; Forfeited amount in respect of Gupta's shares ₹1,500; Amount transferred to Capital Reserve ₹1,600]

Q. 39. Journalise the following transactions in the books of Poonam Ltd. :

200 shares of ₹10 each issued at a premium of ₹5 each payable with allotment were forfeited for the non payment of allotment money of ₹8 per share including premium. The first and final call on these shares at ₹3 per share was not made. The forfeited shares were re-issued @ ₹12 per share fully paid up.

[**Ans.** Transfer to Capital Reserve A/c ₹800.]

Q. 40. Give journal entries for forfeiture and re-issue of shares :

(*a*) *X* Ltd. forfeited 500 shares of ₹10 each, ₹8 called-up on which Vimal has paid application and allotment money of ₹6 per share. Of these, 400 shares were re-issued to Kamal as fully paid for ₹9 per share.

(*b*) *Z* Ltd. forfeited 1,000 shares of ₹10 each issued at 30% premium to Kavita (₹8 called-up) on which she did not pay ₹5 of allotment (including premium) and first call of ₹3. Out of these, 400 shares were re-issued to Savita as ₹8 called-up for ₹6 per share and 300 shares to Namita as fully paid-up for ₹11 per share at different intervals of time.

[**Ans.** Capital Reserve (*a*) ₹2,000; (*b*) ₹400 in first case and ₹900 in second case.]

Q. 41. Vaibhav Ltd. issued 20,000 equity shares of ₹100 each at ₹250 payable as follows :

	₹	
On Application	100	(including premium ₹60)
On Allotment	50	(including premium ₹30)
On First Call	70	(including premium ₹40)
On Second & Final Call	30	(including premium ₹20)

All amounts were received except first and second & final call on 750 shares held by Mr. Akash. His shares were forfeited and 2/3 rd of these shares were reissued to Mr. Dinesh at ₹200 per share. Pass entries for forfeiture and reissue.

[**Ans.** Transfer to Capital Reserve ₹30,000.]

Over-Subscription and Forfeiture of Shares

Q. 42. Jay Ltd. issued a prospectus inviting applications for 1,00,000 shares of ₹10 each. These shares were issued at par on the following terms :

On application ₹2.50, on allotment ₹2.50, on first call ₹3 and on final call the balance.

Applications were received for 1,35,000 shares. Allotments were made on the following basis :

(*i*) To applicants for 25,000 shares — in full;

(*ii*) To applicants for 60,000 shares — 45,000 shares

(*iii*) To applicants for 50,000 shares — 30,000 shares

All excess amount paid on application is to be adjusted against amount due on allotment.

The shares were fully called and paid-up except the amount of allotment, first and final call not paid by those who applied for 4,000 shares of the group applying for 50,000 shares.

All the shares on which calls were not paid were forfeited by the Board of Directors. 1,800 forfeited shares were re-issued as fully paid on receipt of ₹9 per share.

Prepare Cash Book and Journal entries to record the above.

[**Ans.** Cash received on Allotment ₹1,60,500; Bank Balance ₹10,02,200; Capital Reserve ₹5,700.]

Q. 43. *XY* Ltd. invited applications for 5,00,000 Equity shares of ₹10 each, payable as ₹3 on application, ₹4 on allotment and the balance on first and final call. Applications were received for 12,00,000 shares and the shares were allotted on a pro rata basis. The excess application money was to be adjusted against allotment only. *R*, a shareholder, who had applied for 6,000 shares, failed to pay the call money and his shares were accordingly forfeited and reissued at ₹9 per share as fully paid. Pass necessary journal entries.

[**Ans.** Amount received on Ist & Final Call ₹14,92,500; Capital Reserve ₹15,000.]

Hints (*i*) Shares allotted to *R* : 2,500.

(*ii*) There would be no entry for receipt of allotment money.

Q. 44. A company issued 10,000 shares of ₹10 each at a premium of ₹1 per share, payment to be made as follows :

	₹
On Application	3
On Allotment	4 (including premium)
On First call	2
On Second and final call	2

Applications were received for 20,000 shares. Applications for 5,000 shares were rejected and allotment was made proportionately to the remaining applicants. The directors made both the calls and all the money were received, except the allotment, first call and final call on 400 shares, which were subsequently forfeited. Later, 300 of the forfeited shares were re-issued as fully paid @ ₹15 per share. Give journal entries to record the above. Also prepare the Balance Sheet.

[**Ans.** Bank Balance ₹1,11,900; Share Capital ₹99,000; Securities Premium Reserve ₹11,100; Capital Reserve ₹1,350; Balance left in Share Forfeiture A/c ₹450.]

Hint : Securities Premium Reserve Account has been debited in the entry of forfeiture because it is assumed that entire excess application money received on forfeited shares is utilised for share capital.

Q. 45. A company issued for public subscription 60,000 equity shares of ₹10 each at a premium of ₹4 per share, payable as under : ₹4 on Application; ₹5 on Allotment (including premium), ₹2.50 on First Call and ₹2.50 on Final Call.

Applications were received for 75,000 equity shares. The shares were allotted *pro-rata* to the applicants for 70,000 shares, the remaining applications being rejected. Money over-paid on applications was utilised towards sums due on allotment.

A, to whom 1,200 shares were allotted failed to pay allotment and calls money and *B*, to whom 1,800 shares were allotted failed to pay two calls. These shares were subsequently forfeited after the final call was made. All the forfeited shares were sold to Rajesh as fully paid-up at ₹11 per share.

Prepare Cash Book and journal entries required to record the above transactions.

[**Ans.** Amount received on Allotment ₹2,54,800; Capital Reserve ₹14,600. Bank Balance ₹8,52,800.]

Hint : Premium of ₹4,800 due on *A*'s shares will be debited in the entry of forfeiture.

Q. 46. Suzuki Limited issued a prospectus inviting applications for 60,000 shares of ₹10 each at a premium of 30% payable as follows : On Application ₹3.50; On Allotment ₹5.50 (including premium) : On First Call ₹2 and on Second Call ₹2.

Applications were received for 95,000 shares and allotment was made *pro-rata* to applicants of 80,000 shares. Money over-paid on applications were employed on account of sums due on allotment.

X, to whom 1,500 shares were allotted failed to pay the allotment money and on his subsequent failure to pay the First Call his shares were forfeited. *Y*, the holder of 2,400 shares failed to pay the two calls and his shares were forfeited after the Second Call. Of the shares forfeited, 3,000 shares were sold to *Z* as fully paid, *Z* paying ₹8.50 per share, the whole of *Y*'s share being included.

Give journal entries, prepare Bank Account and Balance Sheet.

[**Ans.** Cash received on allotment ₹2,53,500; Balance of Share Forfeiture Account ₹4,200; Capital Reserve ₹12,700; Securities Premium Reserve ₹1,75,500; Cash at Bank ₹7,83,400; Balance Sheet Total ₹7,83,400.]

Hint : Securities Premium Reserve A/c will be debited at the time of forfeiture of *X*'s shares.]

Q. 47. Ganga Ltd. issued a prospectus inviting applications for 20,000 shares at a premium of ₹2 per share payable as follows :

On Application	₹5 (including premium)
On Allotment	₹4
On Call	₹3

Applications were received for 30,000 shares and *pro-rata* allotment made on applications for 24,000 shares. Excess money paid on applications for these shares was utilised towards allotment money.

Atul, who applied for 600 shares failed to pay the allotment money and on his subsequent failure to pay the call, his shares were forfeited.

Pass the necessary entries in the books of Ganga Limited.

[**Ans.** Amount received on allotment ₹58,500; Balance of Share Forfeiture A/c ₹2,000.]

Hints : (1) As Atul had applied for 600 Shares,

he must have been allotted $600 \times \dfrac{20{,}000}{24{,}000} = 500$ shares.

(2) Entry for the forfeiture of shares :

Share Capital A/c	Dr.	5,000	
To Calls in Arrears A/c			3,000
To Share Forfeiture A/c			2,000

Q. 48. A company issued for public subscription 40,000 equity shares of ₹10 each at a premium of ₹2 per share payable as under :

On Application	₹3 per share
On Allotment	₹4 per share (including premium)
On First Call	₹2 per share
On Second Call	₹3 per share

Applications were received for 70,000 shares. Allotment was made pro-rata to the applicants for 50,000 shares, the remaining applications being refused. Money overpaid on application was applied towards sum due on allotment. *A*, to whom 1,600 shares were allotted failed to pay the allotment and calls money. *B*, to whom 2,000 shares were allotted failed to pay the two calls. The shares of *A* and *B* were subsequently forfeited after the second call was made. 3,000 of the forfeited shares were re-issued at ₹8 per share fully paid. The re-issued shares included all of *A*'s shares.

Pass journal entries in the books of the company to record the above transactions.

[Ans. Amount received on Allotment ₹1,24,800; Capital Reserve ₹7,000.]

Q. 49. Hindustan Steel Ltd. invited applications for 50,000 equity shares of ₹10 each at a premium of ₹4 per share. The amount was payable as follows :

On Application	₹4 (including premium ₹2)
On Allotment	₹6 (including premium ₹2)
On First and Final Call	Balance

Applications for 60,000 shares were received. Allotment was made to all the applicants on pro-rata basis. Excess application money was adjusted towards sums due on allotment. Ram, to whom 500 shares were allotted, failed to pay allotment and call money. Shyam, to whom 1,000 shares were allotted, failed to pay the call money. These shares were forfeited. Out of the forfeited shares 1,200 shares (including all shares of Shyam) were re-issued at 10% discount as fully paid-up.

Pass the necessary journal entries in the books of the company by opening 'Calls in Arrears A/c' wherever necessary.

[Ans. Amount received on allotment ₹2,57,400; Balance of Share Forfeiture A/c transferred to Capital Reserve ₹560 + ₹6,000 – ₹1,200 = ₹5,360.]

Hint : Entry for the forfeiture of shares :

Share Capital A/c	Dr.	15,000	
Securities Premium Reserve A/c	Dr.	1,000	
To Calls in Arrear A/c			8,600
To Share Forfeiture A/c			7,400

Q. 50. *SK* Ltd. invited applications for issuing 3,20,000 equity shares of ₹10 each at a premium of ₹5 per share. The amount was payable as follows :

On application — ₹3 per share (including premium ₹1 per share)

On allotment — ₹5 per share (including premium ₹2 per share)
On first and final call — Balance.

Applications for 4,00,000 shares were received. Applications for 40,000 shares were rejected and application money refunded. Shares were allotted on pro-rata basis to the remaining applicants. Excess money received with applications was adjusted towards sums due on allotments. Jeevan holding 800 shares failed to pay the allotment money and his shares were immediately forfeited. Afterwards final call was made. Ganesh who had applied for 2,700 shares failed to pay the final call. His shares were also forfeited. Out of the forfeited shares 1,500 shares were re-issued at ₹8 per share fully paid up. The re-issued shares included all the forfeited shares of Jeevan.

Pass necessary Journal entries for the above transactions in the books of the company. *(C.B.S.E. 2016, All India)*

[**Ans.** Amount received on allotment ₹14,76,300; Balance of Share Forfeiture Account transferred to Capital Reserve ₹5,400 – ₹3,000 = ₹2,400.

Hint. Securities Premium Reserve A/c will be debited from ₹1,600 at the time of forfeiture of Jeevan's shares and from ₹4,800 at the time of forfeiture of Ganesh's shares.

Q. 51. Modern Ltd. issued a prospectus inviting applications for 2,00,000 shares of ₹ 10 each at a premium of ₹6 per share, payable as follows :

On Application	₹5 (including premium ₹2)
On Allotment	₹5 (including premium ₹2)
On Ist Call	₹3 (including premium ₹1)
On IInd & Final Call	₹3 (including premium ₹1)

Applications were received for 2,60,000 shares and pro-rata allotment was made to the applicants for 2,50,000 shares. Excess money paid on applications for these shares was utilised towards allotment.

A, who *applied* for 1,000 shares, failed to pay the allotment money and his shares were forfeited after allotment.

B, who *applied* for 1,500 shares, failed to pay the two calls and his shares were also forfeited.

Of the shares forfeited, 1,800 shares were re-issued as fully paid up for ₹15 per share, the whole of *B*'s share being included. Prepare Cash Book, Journal and Balance Sheet.

[**Ans.** Cash at Bank ₹32,12,000; Cash received on allotment ₹7,47,000; Balance of Share Forfeiture A/c ₹850; Capital Reserve ₹9,750; Balance of Securities Premium Reserve A/c ₹12,03,400; Total of Balance Sheet ₹32,12,000.]

Hint. Securities Premium Reserve A/c will be debited from ₹1,600 at the time of forfeiture of *A*'s shares and from ₹2,400 at the time of forfeiture of *B*'s shares.]

Q. 52. Zen Ltd. issued 10,000 equity shares of ₹10 each at a premium of ₹3 per share payable as :

On Application	₹4
On Allotment	₹5 (including premium)
On First Call	₹2

The balance as and when required.

The public applied for 12,000 shares. The company made pro-rata allotment to all the applicants. One shareholder who was allotted 900 shares paid the entire amount with allotment while another shareholder who had applied for 1,200 shares, failed to pay the allotment money and on his subsequent failure to pay the first call his shares were forfeited.

Of the forfeited shares, 800 were reissued at ₹7 per share.

You are required to prepare :

(*i*) Share Allotment Account,

(*ii*) Securities Premium Reserve Account,

(*iii*) Share Forfeiture Account, and

(*iv*) Calls-in-Arrears Account. *(I.S.C. Specimen Question Paper, 2018)*

[**Ans.** Amount received on allotment ₹37,800; Balance of Securities Premium Reserve A/c ₹27,000; Balance of Share Forfeiture A/c ₹960; Calls in Arrears ₹6,200]

Q. 53. Suprabhat Ltd. invited applications for issuing 5,00,000 equity shares of ₹10 each payable as follows :

On application and allotment ₹7 per share (including premium ₹4),

On first call ₹4 per share,

On second and final call ₹3 per share.

Applications for 6,00,000 shares were received and pro-rata allotment was made to all the applicants. Excess application money was adjusted on the sums due on calls. A shareholder who had applied for 18,000 shares did not pay the first, and the second and final call. His shares were forfeited. One-third of the forfeited shares were reissued as fully paid at 5% discount.

Pass necessary journal entries for the above transactions in the books of the company.

[**Ans.** Amount received on first call ₹12,61,000 Capital Reserve ₹19,500.]

Q. 54. A limited company forfeited 400 shares of Mr. *X*, who had applied for 600 shares on account of non-payment of allotment money ₹3 + ₹2.50 (premium) and first call ₹2. Only ₹4 per share was received with application. Out of these, 200 shares were re-issued to Mr. *Y* at ₹8 per share, ₹9 paid-up.

Give journal entries relating to forfeiture and re-issue.

[**Ans.** Capital Reserve ₹1,000.]

Q. 55. *AB* Ltd. invited applications for issuing 1,00,000 equity shares of ₹10 each. The amount was payable as follows :

On Application	₹3 per share
On Allotment	₹3 per share
On First and Final Call	₹4 per share

Applications for 1,50,000 shares were received and pro-rata allotment was made to all applicants as follows :

Applicants for 80,000 shares were allotted 60,000 shares on pro-rata basis.

Applicants for 70,000 shares were allotted 40,000 shares on pro-rata basis.

Sudha, to whom 600 shares were allotted out of the group applying for 80,000 shares failed to pay the allotment money. Her shares were forfeited immediately after allotment.

Asha, who had applied for 1,400 shares out of the group applying for 70,000 shares failed to pay the first and final call. Her shares were also forfeited.

Out of the forfeited shares 1,000 were re-issued @ ₹8 per share fully paid-up. The re-issued shares included all the forfeited shares of Sudha.

Pass necessary journal entries to record the above transactions.

[**Ans.** Amount received on allotment ₹1,48,800. Amount received on first call ₹3,94,400. Amount transferred to Capital Reserve ₹2,800.]

Q. 56. *R* Ltd. invited application for 3,00,000 shares of ₹10 each, payable as follows :

	₹
On Application	3
On Allotment	5
On First and Final Call	2

Application were received for 4,80,000 shares and the allotment was made as follows :

Category	*Shares Applied for*	*Shares Allotted*
I	40,000	30,000
II	3,00,000	2,00,000
III	1,40,000	70,000

All the shares were allotted on pro-rata basis and excess application money was adjusted towards sum due on allotment.

Archna, who belonged to category I and who had applied for 1,200 shares, failed to pay the allotment money. Her shares were forfeited immediately after allotment was not received. Deepali, who belonged to Category II and who had applied for 600 shares, failed to pay the final call money. Her shares were forfeited after the final call. The forfeited shares were re-issued @ ₹8 per share fully paid up.

Pass necessary journal entries in the books of *R* Ltd.

[**Ans.** Amount received on allotment ₹9,56,400; Amount received on first call ₹5,97,400; Amount transferred to Capital Reserve ₹4,200.]

Q. 57. *X* Ltd. invited applications for 4,00,000 shares of ₹10 each. The shares were issued at a premium of ₹7 per share. The amount was payable as follows :

On Application & Allotment : ₹9 per share (including premium ₹4)
On First & Final Call : The balance amount (including premium)

Applications were received for 5,70,000 shares and the allotment was made as under :

(*i*) To applicants for 3,50,000 shares : 2,50,000 shares on pro-rata basis
(*ii*) To applicants for 2,00,000 shares : 1,50,000 shares on pro-rata basis
(*iii*) To applicants for 20,000 shares : NIL

Excess application and allotment money could be utilized for calls.

A, who belonged to the first category and was allotted 500 shares, failed to pay the first call money. *B*, who belonged to the second category and was allotted 300 shares also failed to pay the first call money. Their shares were forfeited and were re-issued @ ₹15 per share fully paid-up.

Pass necessary Cash-Book and Journal entries.

[**Ans.** Cash received on first call ₹18,46,300; Capital Reserve ₹6,700; Cash at Bank ₹68,08,300.]

Note. It has been assumed that the entire excess application and allotment money is exclusively for share capital and hence 'Securities Premium Account' has been debited in the entry for forfeiture.

Q. 58. Durga Ltd. invited applications for issuing 1,00,000 equity shares of ₹10 each at par. The amount was payable as follows :

On Application	₹2 per share.
On Allotment	₹3 per share.
On First and Final Call	₹5 per share.

Applications were received for 2,80,000 shares. Applications for 30,000 shares were rejected and the money refunded. Allotment was made to the remaining applicants as follows.

Category	*No. of Shares Applied*	*No. of Shares Allotted*
I	1,50,000	85,000
II	1,00,000	15,000

Excess money received with applications was adjusted towards sums due on allotment and first and final call. All calls were made and were duly received except the final call by a shareholder belonging to Category I who has applied for 300 shares. His shares were forfeited. The forfeited shares were re-issued at a premium of 30% fully paid up.

Pass necessary Journal entries for the above transactions in the book of Durga Ltd. Open calls in-arrears and calls in advance account wherever required.

[**Ans.** Net amount received on allotment ₹1,25,000; Net amount received on final call ₹4,24,150; Capital Reserve ₹850.]

Hint : Excess application money transferred to Share Allotment A/c : ₹1,75,000
Excess application money transferred to Calls in Advance A/c : ₹75,000
Excess application money returned ₹1,10,000
Calls in Arrears ₹850.

Q. 59. Piyush Ltd. invited applications for issuing 1,00,000 shares of ₹10 each payable as follows:

₹4 — per share on application

₹2 — per share on allotment

Balance on first and final call.

Applications were received for 1,60,000 shares. Full allotment was made to the applicants of 10,000 shares. The remaining applicants were allotted 90,000 shares on pro-rata basis. Excess money received with application was adjusted towards sums due on allotment and call.

Kanika, holding 6,000 shares, who belonged to the category of applicants to whom full allotment was made, paid the call money at the time of allotment. Ruchi, who belonged to the category of applicants to whom shares were allotted on pro-rata basis did not pay anything after application on her 600 shares. Ruchi's shares were forfeited after the first and final call. These shares were later reissued at ₹9 per share fully paid up.

Pass the necessary journal entries for the above transactions by opening calls in arrears and calls in advance account wherever necessary.

[Ans. Amount received on first & final call ₹3,14,000; Calls in Arrear ₹2,000; Capital Reserve ₹3,400]

Hints : (*i*) Excess application money transferred to Calls in Advance A/c : ₹60,000

(*ii*)

		₹
Amount due from Ruchi on First and Final Call = 600 × ₹4	=	2,400
Less : Calls in Advance from Ruchi		400
Amount not paid by Ruchi on First & Final Call		2,000

Utilisation of excess application money for Securities Premium

Q. 40. Khushboo Ltd. issued for Public subscription 50,000 equity shares of ₹10 each at a premium of 30% payable as under :

₹4	on application
₹5	on allotment (including premium)
₹4	on first & final call

Applications were received for 1,00,000 shares. Allotment was made *pro-rata* to the applicants for 80,000 shares, the remaining applications being refused. Money overpaid on application was utilised towards sums due on allotment.

Chatterjee, to whom 1,000 shares were allotted, failed to pay the allotment and call money and the shares were subsequently forfeited. Half of the forfeited shares were reissued as fully paid at a discount of 10%. Show the journal entries to record the above transactions.

[Ans. Amount received on allotment ₹1,27,400; Capital Reserve ₹2,500.]

Hints :

(*i*) Out of excess application money of ₹2,400, the amount of ₹2,000 is a part of share capital and balance of ₹400 is a part of securities premium.

(*ii*) Entry for forfeiture of shares :

Equity Share Capital A/c	Dr.	10,000	
Securities Premium Reserve A/c (3,000 – 400)	Dr.	2,600	
To Calls in Arrears A/c			6,600
To Share Forfeiture A/c			6,000

Q. 41. Kochi Silk Ltd. issued a prospectus inviting applications for 40,000 shares of ₹10 each at a premium of ₹8 per share, payable as follows :

On Application	₹6 (including ₹2 premium)
On Allotment	₹6 (including ₹2 premium)
On First Call	₹3 (including ₹2 premium)

On Second & Final Call ₹3 (including ₹2 premium)

Applications were received for 80,000 shares and pro-rata allotment was made on the applications for 70,000 shares. It was decided to utilise excess application money towards the sums due on allotment.

X, to whom 1,200 shares were *allotted,* failed to pay the allotment money and on his subsequent failure to pay the first call his shares were forfeited.

Y, who *applied* for 3,500 shares failed to pay the two calls and on his such failure, his shares were also forfeited.

Of the shares forfeited, 2,500 shares were reissued as fully paid up for ₹9 per share, the whole of *Y*'s shares being included. Prepare Cash Book and Journal entries.

[**Ans.** Cash at Bank ₹7,21,500; Net amount received on allotment ₹58,200; Capital Reserve ₹17,500.]

Hints :

(*i*) Out of excess application money of ₹5,400, an amount of ₹4,800 is a part of share capital and the balance of ₹600 is a part of securities premium reserve.

(*ii*) Entry for forfeiture of *X*'s shares :

Share Capital A/c (1,200 × ₹9)	Dr.	10,800	
Securities Premium Reserve A/c (1,200 × ₹4 = ₹4,800 – ₹600)	Dr.	4,200	
To Calls in Arrears A/c			5,400
To Share Forfeiture A/c			9,600

Q. 62. Jupiter Ltd. issued shares of ₹100 each at a premium of 40% payable as follows :

On Application	₹50
On Allotment	₹70 (including premium)
On First & Final Call	₹20

Vinita, who applied for 700 shares and to whom 400 shares were allotted on prorata basis did not pay allotment and her shares were immediately fofeited. Pass entry for forfeiture of shares.

[**Ans.** Amount credited to Share Forfeiture Account ₹32,000.]

Hint : Securities Premium Reserve A/c will be debited by ₹13,000 in the entry for forfeiture of shares.

Additional Questions (For Practice)

Q. 63. On 1st April, 2019 Vivek Ltd. was formed with an authorized capital of ₹1,00,00,000 divided into 2,00,000 equity shares of ₹50 each. The company issued prospectus inviting applications for 1,80,000 shares. The issue price was payable as under :

On Application	:	₹15
On Allotment	:	₹20
On Call	:	Balance amount

The issue was fully subscribed and the company allotted shares to all the applicants. All money was received except allotment on 5,000 shares. The company did not make the call during the year.

Show the following :

(*a*) Share capital in the Balance Sheet of the company as per Schedule-III Part-I of the Companies Act, 2013.

(*b*) Also prepare 'Notes to Accounts' for the same.

[**Ans.** Subscribed but not Fully Paid Capital ₹62,00,000.]

Q. 64. Pass necessary journal entries for the following transactions in the books of Gopal Ltd. :

(*i*) Purchased furniture for ₹2,50,000 from M/s Furniture Mart. The payment to M/s Furniture Mart was made by issuing equity shares of ₹10 each at a premium of 25%.

(*ii*) Purchased a running business from Aman Ltd. for a sum of ₹15,00,000. The payment of ₹12,00,000 was made by issue of fully paid equity shares of ₹10 each and balance by a bank draft. The assets and liabilities consisted of the following :

Plant ₹3,50,000; Stock ₹4,50,000; Land and Building ₹6,00,000; Sundry Creditors ₹1,00,000.

[**Ans.** (*i*) Number of shares issued 20,000 (*ii*) Goodwill ₹2,00,000.]

Forfeiture of Shares Issued at Par

Q. 65. *Y* Ltd. invited applications for issuing 15,000 equity shares of ₹10 each on which ₹6 per share were called up, which were payable as follows :

On application	₹2 per share
On allotment	₹1 per share
On first call	₹3 per share

The issue was fully subscribed and the amount was received as follows :

On 10,000 shares	— ₹6 per share
On 3,000 shares	— ₹3 per share
On 2,000 shares	— ₹2 per share

The directors forfeited those shares on which less than ₹6 per share were received. The forfeited shares were re-issued at ₹9 per share, as ₹6 per share paid up.

Pass necessary journal entries for the above transactions in the books of the company.

[**Ans.** Amount received on allotment ₹13,000; Amount received on first call ₹30,000; Capital Reserve ₹13,000.]

Forfeiture of Shares Issued at Premium

Q. 66. *XYZ* Limited has an Authorised Capital of ₹4,00,000 divided into shares of ₹20 each, the whole of which is issued and subscribed at a premium of ₹2 per share. The amount was payable as follows : On Application and Allotment: ₹10 per share; On Ist Call ₹4 per share (including premium) and the balance as and when required.

The company made both the calls. The application and allotment money was duly received. But a shareholder holding 2,000 shares failed to pay both the calls and his shares were forfeited. These shares were later re-issued at ₹14 per share as fully paid.

Give journal entries regarding the above.

[Ans. Capital Reserve ₹8,000.]

Hint : In this question ₹10 has been called on application and allotment jointly, therefore, following entries will be passed for application and allotment :

Bank A/c	Dr.	2,00,000	
To Share Application & Allotment A/c			2,00,000
Share Application & Allotment A/c	Dr.	2,00,000	
To Share Capital A/c			2,00,000

Q. 67. The Mohan Ltd., has authorised capital of ₹5,00,000 divided into 50,000 shares of ₹10 each. The company issued a prospectus inviting applications for 30,000 shares of ₹10 each at a premium of ₹2 per share, payable as follows : On Application ₹3; On Allotment ₹5 (including premium); On First Call ₹2 ; On Second and Final Call ₹2.

The Company received applications for 45,000 shares and *pro-rata* allotment was made in respect of applications of 40,000 shares and the remaining applications were rejected. Money overpaid on applications was employed on account of sums due on allotment. All the calls were made.

B, to whom 300 shares were allotted failed to pay the two calls. The company decided to forfeit the shares allotted to *B*. These shares were subsequently re-issued to *C* as fully paid for ₹9 per share.

Pass the necessary journal entries in the books of the company and prepare the Opening Balance Sheet.

[Ans. Bank balance ₹3,61,500; Capital Reserve ₹1,500; Balance Sheet Total ₹3,61,500.]

Q. 68. *A* Ltd. forfeited 800 shares of ₹10 each issued at 20% premium (to be paid at the time of allotment) for non-payment of a final call of ₹2 per share. Out of these, 600 shares were re-issued as fully paid-up for ₹13 per share. Journalise.

[Ans. Capital Reserve ₹4,800.]

Q. 69. *B* Ltd. forfeited 500 shares of ₹10 each issued at 20% premium (to be paid at the time of allotment) for non-payment of the first call of ₹3 per share and final call of ₹2 per share. Out of these, 300 shares were re-issued as fully paid-up for ₹10 per share. Journalise.

[Ans. Capital Reserve ₹1,500.]

Q. 70. *C* Ltd. forfeited 300 shares of ₹10 each issued at 20% premium (to be paid at the time of allotment) for non-payment of allotment money of ₹4 per share (including premium), first call of ₹3 per share and final call of ₹2 per share. Out of these, 200 shares were re-issued as fully paid-up at a discount of ₹3 per share. Journalise.

[Ans. Capital Reserve : Nil.]

Q. 71. *X* Ltd. forfeited 800 shares of ₹20 each issued at a premium of ₹2 per share to Mahesh (₹18 called-up) on which he did not pay first call of ₹4. Of these, 300 shares were re-issued @ ₹15 per share as ₹18 paid-up. Journalise.

[**Ans.** Capital Reserve ₹3,300.]

Q. 72. *X* Ltd., forfeited 1,000 shares of ₹20 each issued at a premium of ₹2 per share to Ashok (₹18 called-up) on which he did not pay allotment of ₹6 (including premium) and Ist Call of ₹4. Give Journal Entries for forfeiture and re-issue in the following cases :

(*i*) 600 shares were re-issued to Mohan at ₹14 per share as ₹18 paid up; (*ii*) 200 shares to Sohan as fully paid-up for ₹24 per share; and (*iii*) 200 shares to Suresh as fully paid-up for ₹10 per share at different intervals of time.

[**Ans.** Amount transferred to Capital Reserve (*i*) ₹3,600; (*ii*) ₹2,000 and (*iii*) Nil.]

Q. 73. *X* Limited forfeited 1,000 shares of ₹10 each (₹8 called-up) issued at a premium of ₹2 per share to Mr. *R*, for non-payment of allotment money of ₹5 per share (including premium). Out of these, 700 shares were re-issued to Mr. Sanjay as ₹8 called for ₹7 per share. Give the necessary Journal entries relating to forfeiture and re-issue of shares.

[**Ans.** Capital Reserve ₹2,800.]

Q. 74. *Y* Ltd. forfeited 100 shares of ₹10 each issued at 20% premium (to be paid at the time of allotment) on which first call money of ₹3 was not received; the final call money of ₹2 is not yet called. These shares were subsequently re-issued at ₹7 per share as ₹8 paid-up. Give necessary journal entries regarding forfeiture and re-issue of shares.

[**Ans.** Capital Reserve ₹400.]

Q. 75. *Y* Ltd. forfeited 2,000 shares of ₹10 each issued at 20% premium (to be paid at the time of allotment) on which allotment money of ₹4 (including premium) and first call money of ₹3 was not received; the final call money of ₹2 is not yet called. 1,500 of these shares were re-issued as fully paid for ₹7 per share. Journalise.

[**Ans.** Capital Reserve Nil.]

Hint : No entry will be passed for transferring the Share Forfeiture A/c to Capital Reserve A/c.

Q. 76. *Z* Ltd. forfeited 1,200 shares of ₹100 each, issued at a premium of 30% to Dinesh on which he had paid application money of ₹50 per share and allotment money of ₹50 per share (including premium), for non-payment of a first call of ₹10 per share. Out of these, 500 shares were re-issued as fully paid for ₹105 per share. Journalise.

[**Ans.** Capital Reserve ₹35,000.]

Q. 77. *Z* Ltd. forfeited 700 shares of ₹100 each, issued at a premium of 30% to Ghanshyam on which he had paid application money of ₹35 per share, for non-payment of allotment money of ₹50 per share (including premium) and first call of ₹15 per share. Out of these, 400 shares were re-issued as ₹70 paid-up for ₹65 per share. Journalise.

[**Ans.** Capital Reserve ₹12,000.]

Q. 78. 500 shares of ₹10 each, issued at a premium of ₹1 on which ₹8 (including premium) was called and ₹6 (including premium) was paid, have been forfeited. 400 of these shares were re-issued as fully paid in such a way that ₹800 were transferred to Capital Reserve. Journalise.

[**Ans.** Reissue Price ₹7 per share.]

Hint : Entry for forfeiture will be :

Share Capital A/c	Dr.	3,500	
To Calls in Arrears A/c			1,000
To Share Forfeiture A/c			2,500

Q. 79. On April 1, 2022 the Directors of Ashoka Metals Ltd. issued 60,000 equity shares of ₹10 each at ₹12 per share, the amount payable as ₹5 on application (including premium), ₹4 on allotment and the balance on July 15, 2022.

On April 10, 2022 applications were received for 80,000 shares. Of the cash received in excess, ₹40,000 were returned and ₹60,000 were applied towards the amount due on allotment. The balance of allotment money was received on April 30, 2022. All the shareholders paid the call due on July 15, 2022, with the exception of one shareholder holding 500 shares. These shares were forfeited on August 31, 2022.

You are required to submit Journal Entries regarding the above transactions and also prepare the Balance Sheet of the Company on August 31, 2022.

[**Ans.** Balance at Bank ₹7,18,500; Balance of Share Forfeiture a/c ₹3,500; Share Capital A/c ₹5,98,500. B/S total ₹7,18,500.]

Hint : Applicants for 8,000 shares were not allotted any shares and the applicants for 72,000 shares were allotted 60,000 shares.

Share Application A/c	Dr.	4,00,000	
To Share Capital A/c			1,80,000
To Securities Premium Reserve A/c			1,20,000
To Share Allotment A/c			60,000
To Bank A/c			40,000

Q. 80. Mahadev Ltd. with an authorised capital of ₹5,00,000 divided into 50,000 equity shares of ₹10 each, issues the entire amount of the shares payable as follows :

₹5 on Application (including premium of ₹3 per share)
₹4 on Allotment, and
₹4 on Call.

All share money is received in full with the exception of the allotment on 200 shares and the call money on 500 shares (including the 200 shares on which the allotment money has not been paid).

The above 500 shares are duly forfeited and 400 of these (including the 200 shares on which allotment money has not been paid) are re-issued at ₹8 per share as fully paid up. Pass journal entries (including cash transactions) and show the balances in the Balance Sheet giving effect to the above transactions.

[**Ans.** Share Capital ₹4,99,600; Capital Reserve ₹800; Securities Premium Reserve ₹1,50,000; Cash at Bank ₹6,50,400.]

Q. 81. R.K. Ltd. invited applications for issuing 70,000 Equity Shares of ₹10 each at a premium of ₹35 per share. The amount was payable as follows :

On Application	₹15 (including ₹12 premium)

On Allotment	₹10 (including ₹8 premium)
On First and Final Call	Balance

Applications for 65,000 shares were received and allotment was made to all the applicants. A shareholder, Ram, who was allotted 2,000 shares, failed to pay the allotment money. His shares were forfeited immediately after allotment. Afterwards, the first and final call was made. Sohan, who had 3,000 shares, failed to pay the first and final call. His shares were also forfeited. Out of the forfeited shares, 4,000 shares were re-issued at ₹50 per share fully paid up. The re-issued shares included all the shares of Ram.

Pass necessary journal entries for the above transactions in the books of R.K. Ltd.

[**Ans.** Forfeited amount in respect of Ram's shares ₹6,000; Forfeited amount in respect of Sohan's shares ₹15,000; Amount transferred to Capital Reserve ₹16,000 (₹6,000 in respect of Ram's shares and ₹10,000 in respect of Sohan's shares).

Q. 82. Denspar Ltd. invited applications for issuing 2,00,000 equity shares of ₹10 each at a premium of ₹20 per share. The amount was payable as follows :

On Application — ₹ 2 per share
On Allotment — ₹13 per share (including ₹10 premium)
On First Call — ₹ 7 per share (including ₹5 premium)
On Final Call — ₹ 8 per share (including ₹5 premium)

Applications for 1,80,000 shares were received. Shares were allotted to all the applicants. Yogesh, a shareholder holding 5,000 shares paid his entire share money along with the allotment money. Vishesh, a holder of 7,000 shares, failed to pay the allotment money. Afterwards the first call was made. Vishesh paid the allotment money along with the first call money. Samyesh, holding 2,000 shares did not pay the final call. Samyesh's shares were forfeited immediately after the final call. Out of the forfeited shares, 1,500 shares were reissued at ₹8 per share fully paid up.

Pass the necessary journal entries for the above transactions in the books of Denspar Ltd. *(C.B.S.E. 2019, Rajasthan)*

[**Ans.** Transfer to Capital Reserve ₹7,500.]

Over-Subscription and Forfeiture of Shares

Q. 83. Nitro Paints Ltd. invited applications for issuing 1,60,000 equity shares of ₹10 each at a premium of ₹3 per share. The amount was payable as follows :

On application — ₹6 per share (including premium ₹1)
On allotment — ₹3 per share (including premium ₹1)
the balance — on first and final call

Applications for 1,80,000 shares were received. Applications for 10,000 shares were rejected and pro-rata allotment was made to the remaining applicants. Over payment on application were adjusted towards sums due on allotment. All calls were made and were duly received except allotment and final call from Aditya who was allotted 3,200 shares. His shares were forfeited. Half of the forfeited shares were re-issued for ₹43,000 as fully paid up.

Pass necessary journal entries for the above transactions in the books of Nitro Paints Ltd. *(C.B.S.E. 2017, Comptt. Delhi)*

[**Ans.** Amount received on allotment ₹4,11,600; Capital Reserve ₹8,600.]

Hint : Securities Premium Reserve A/c will be debited from ₹6,400 at the time of forfeiture of shares.

Q. 84. *D* Ltd. offered to the public 20,000 shares of ₹100 each at a premium of ₹20 per share payable as follows :

	₹
On Application	30
On Allotment	40 (including premium)
On First Call	25, and
On Final Call	25

Applications were received for 26,000 shares out of which those for 1,000 shares were rejected outright; full allotment was made to the applicants for 5,000 shares and *pro-rata* allotment was made to balance.

Final Call was not made and a shareholder holding 600 shares to whom allotment was made on *pro-rata* basis failed to pay the allotment and first call money. His shares were forfeited. Out of these, 500 shares were re-issued at ₹70 per share as ₹75 paid-up.

Prepare Cash Book, Journal entries and the Balance Sheet of the company.

[**Ans.** Bank Balance ₹19,02,000; Share Capital ₹14,92,500; Securities Premium Reserve ₹3,88,000; Capital Reserve ₹17,500; Balance left in Share Forfeiture A/c ₹4,000; B/S total ₹19,02,000.]

Q. 85. A Limited company invites applications for 50,000 equity shares of ₹10 each payable as follows :

On Application	₹3
On Allotment	₹4
On First Call	₹2
On Final Call	Balance

Applications were received for 70,000 shares. Allotments were made on the following basis :

(*i*) To applicants for 10,000 shares — in full.

(*ii*) To applicants for 60,000 shares — 40,000 shares

Excess money paid on application was utilised towards allotment money.

A shareholder who was allotted 1,000 shares out of the group applying for 60,000 shares failed to pay allotment money and money due on calls. These shares were forfeited. 600 forfeited shares were re-issued as fully paid on receipt of ₹8 per share.

Prepare Cash Book and journal entries in the books of company.

[**Ans.** Bank Balance ₹4,99,300; Amount received on allotment ₹1,37,500; On First Call ₹98,000 and on Final Call ₹49,000; Amount transferred to Capital Reserve ₹1,500.]

Q. 86. *X* Ltd. invited applications for 50,000 Equity Shares of ₹10 each, payable ₹3.50 on application; ₹5 on allotment (including premium ₹2.50); and ₹4 on first and final call.

The company received applications for 65,000 shares. It was decided :

(*a*) to refuse allotment to the applicants for 5,000 shares;

(*b*) to allot in full to the applicants for 20,000 shares;

(*c*) to allot balance of the available shares *pro-rata* among the other applicants; and (*d*) to utilise the excess application money in part payment of allotment money.

All the money due was received except from one applicant to whom shares had been allotted on *pro-rata* basis. He failed to pay allotment and call money and his 300 shares were forfeited. These shares were re-issued at ₹9 as fully paid.

Give journal entries to record the above transactions in the books of the company.

[Ans. Cash received on Allotment ₹2,13,850; Balance of Share Forfeiture A/c transferred to Capital Reserve ₹1,400 – ₹300 = ₹1,100.]

Q. 87. New Industries Limited issued a prospectus, inviting applications for 1,00,000 shares of ₹10 each at a premium of ₹5 per share, payable as follows : On Application ₹4.50; On Allotment ₹7.50 (including Premium); On Ist Call ₹2.00 and On Final Call ₹1.00.

Applications were received for 1,25,000 shares and allotment was made *pro-rata* to the applicants of 1,20,000 shares, the remaining applications being refused. Money received in excess on the application was adjusted towards the amount due on allotment.

D, to whom 2,000 shares were allotted, failed to pay allotment money and on his failure to pay the first call, his shares were forfeited. *M*, the holder of 3,000 shares, failed to pay the two calls, and so his shares were also forfeited. All these shares were sold to *R*, credited as fully paid for ₹8 per share.

Pass Cash Book and journal entries (with narrations) to record the above issue of shares by the company.

[Ans. Cash at Bank ₹15,11,800; Cash received on allotment ₹6,46,800; Balance of Share Forfeiture A/c transferred to Capital Reserve ₹10,800 + ₹21,000 – ₹10,000 = ₹21,800.]

Q. 88. *X* Limited offered to the public 10,000 equity shares of ₹10 each at a premium of ₹2 per share payable as follows :

On application ₹3; On allotment (including premium) ₹4; On first call ₹3 and on second and final call ₹2.

Applications were received for 15,000 shares.

All applications were placed under four categories and allotment was made as follows :

Category *A* : to applicants of 4,000 shares	in full
Category *B* : to applicants of 6,000 shares	4,000 shares
Category *C* : to applicants of 3,000 shares	2,000 shares
Category *D* : to applicants of 2,000 shares	Nil

Except in the cases where applications were wholly rejected, excess application money was not to be refunded but to be adjusted against moneys due on allotment and calls.

A, an applicant under category *B* to whom 400 shares were allotted failed to pay the allotment money and on his failure to pay the first call his shares were forfeited.

B, an applicant under category *C* to whom 300 shares were allotted failed to pay both the calls and his shares were also forfeited.

500 of the shares thus forfeited were re-issued to *C* as fully paid for ₹8 per share.

Show Cash Book, Journal entries and prepare the Balance Sheet in the books of the company; you are to assume that the whole of the *A*'s shares were issued to *C*.

[**Ans.** Cash received on allotment ₹30,000; Balance of Share Forfeiture A/c ₹1,000; Capital Reserve ₹1,300; Securities Premium Reserve ₹19,200; Cash at Bank ₹1,19,500; Balance Sheet Total ₹1,19,500.]

Hint : Premium will be debited at the time of forfeiture of *A*'s Shares.

Q. 89. Premier Tools Ltd. invited applications for issuing 2,00,000 equity shares of ₹10 each at a premium of ₹2 per share. The amount was payable as follows :

On Application — ₹5 per share (including premium)
On Allotment — ₹3 per share
On First & Final Call — Balance

Applications were received for 2,50,000 shares. Applications for 10,000 shares were rejected and pro-rata allotment was made to the remaining applicants. Over payments received on application were adjusted towards sums due on allotment.

All calls were made and duly received except allotment and first and final call from Naveen who applied for 7,200 shares. His shares were forfeited. Half of the forfeited shares were reissued for ₹48,000 as fully paid.

Pass the necessary journal entries for the above transactions in the books of Premier Tools Ltd. Open calls-in-arrears account wherever required.

(C.B.S.E. 2020, Delhi)

[**Ans.** Amount received on allotment ₹3,88,000. Transfer to Capital Reserve ₹12,000]

Q. 90. *X* Ltd. invited applications for issuing 80,000 equity shares of ₹10 each at a premium of ₹2 per share. The amount was payable as follows :

On application ₹6 (including premium) per share.

On allotment ₹3 per share.

Balance on first and final call.

Applications for 90,000 shares were received. Applications for 5,000 shares were rejected and *pro-rata* allotment was made to the remaining applicants. Over payments received on application was adjusted towards sums due on allotment. All calls were made and were duly received except the allotment and final call on 1,600 shares allotted to Vijay. These shares were forfeited and the forfeited shares were re-issued for ₹18,400 fully paid up.

Pass necessary journal entries in the books of the company.

[**Ans.** Amount received on allotment ₹2,05,800; Capital Reserve ₹7,000]

Q. 91. *A* Ltd. forfeited 400 shares of Mr. *X* who had applied for 600 shares on account of non-payment of allotment, first call and final call. Shares were issued at ₹2 premium payable as follows :

On Application ₹3, on Allotment ₹3 + 2, on First call ₹2 and Final Call ₹2. Out of these, 300 shares were re-issued to Mr. *Y* at the rate of ₹12 per share as fully paid shares. Give journal entries in the books of company to record above transactions.

[**Ans.** Capital Reserve ₹1,350.]

Q. 92. *K* Limited has been registered with an authorised capital of ₹20,00,000 divided into 20,000 shares of ₹100 each, of which 10,000 shares were offered for public subscription at a premium of ₹5 per share, payable as under :

	₹
On application	30
On allotment	25 (including premium)
On first call	20
On final call	30

Applications were received for 18,000 shares, of which applications for 3,000 shares were rejected outright; the rest of the applications were allotted 10,000 shares on pro-rata basis. Excess application money was transferred to allotment.

All the moneys were duly received except from Sundar, holder of 200 shares, who failed to pay allotment and first call money. His shares were later forfeited, and re-issued to Shyam at ₹60 per share, ₹70 paid up. Final Call has not been made. Pass necessary Cash Book and Journal entries in the books of *K* Limited.

[**Ans.** Amount received on allotment ₹98,000; Amount transferred to Capital Reserve ₹7,000; Cash at Bank ₹7,56,000.]

Note : Securities Premium Reserve Account has been debited in the entry of forfeiture because it is assumed that the entire excess application money is utilised for share capital.

Q. 93. Jeevan Dhara Ltd. invited applications for issuing 1,20,000 equity shares of ₹10 each at a premium of ₹2 per share. The amount was payable as follows :

On Application — ₹2 per share
On Allotment — ₹5 per share (including premium)
On first and final call — balance

Applications for 1,50,000 shares were received. Shares were allotted to all the applicants on pro-rata basis. Excess money received on applications was adjusted towards sums due on allotment. All calls were made. Manu who had applied for 3,000 shares failed to pay the amount due on allotment and first and final call. Madhur who was allotted 2,400 shares failed to pay the first and final call. Shares of both Manu and Madhur were forfeited. The forfeited shares were re-issued at ₹9 per share as fully paid up.

Pass necessary journal entries for the above transactions in the books of Jeevan Dhara Ltd.

[**Ans.** Amount received on allotment ₹5,29,200; Capital Reserve ₹13,200]

Hint. Security Premium due from Manu ₹4,800 will be debited in the entry for forfeiture.

Q. 94. Ganesh Ltd. issued a prospectus inviting applications for 20,000 shares of ₹10 each at a premium of ₹4 per share, payable as follows :

On Application	₹4 (including premium ₹1)
On Allotment	₹3 (including premium ₹1)
On First Call	₹3 (including premium ₹1)
On Second and Final Call	₹4 (including premium ₹1)

Applications were received for 30,000 shares and pro-rata allotment was made on the applications for 24,000 shares. It was decided to utilise excess application money towards the sums due on allotment.

X, who was *allotted* 500 shares, failed to pay the allotment money and on his subsequent failure to pay the first call, his share were forfeited.

Y, who *applied* for 1,800 shares, failed to pay the two calls and his shares were forfeited after the second call.

Of the shares forfeited, 1,700 shares were re-issued as fully paid up for ₹8 per share, the whole of Y's shares being included.

Prepare Cash Book, Journal and Balance Sheet.

[Ans. Cash at Bank ₹2,78,500; Cash received on allotment ₹42,900; Balance of Share Forfeiture A/c ₹1,140; Capital Reserve ₹4,860; Balance of Securities Premium Reserve A/c ₹75,500; Total of Balance Sheet ₹2,78,500.]

Hints : (*i*) Entry on forfeiture of 500 Shares of X :

Share Capital A/c	Dr.	3,500	
Securities Premium Reserve A/c (₹500 for allotment + ₹500 for Ist Call)	Dr.	1,000	
To Calls in Arrears A/c			2,600
To Share Forfeiture A/c			1,900

(*ii*) Entry on forfeiture of 1,500 Shares of Y :

Share Capital A/c	Dr.	15,000	
Securities Premium Reserve A/c (₹1,500 for Ist Call + ₹1,500 for IInd Call)	Dr.	3,000	
To Calls in Arrears A/c			10,500
To Share Forfeiture A/c			7,500

Q. 93. Vinod Papers Ltd. invited applications for issuing 1,00,000 shares of ₹10 each at a premium of ₹4 per share payable as follows :

On Application	₹4 (including premium ₹2)
On Allotment	₹4 (including premium ₹2)
On First & Final Call	₹6

Applications were received for 1,30,000 shares and pro-rata allotment was made to all applicants as follows :

(*i*) Applicants for 80,000 shares were allotted 60,000 shares, and

(*ii*) Applicants for 50,000 shares were allotted 40,000 shares.

X, who belonged to the first category and was **allotted** 900 shares failed to pay the allotment and call money.

Y, who belonged to the second category and who **applied** for 1,000 shares also failed to pay the allotment and call money. Their shares were forfeited and 1,400 of the forfeited shares were re-issued @ ₹9 per share as fully paid. Re-issued shares included whole of Y's shares.

Prepare Cash Book, journal entries and an opening Balance Sheet.

[Ans. Cash at Bank ₹13,97,600; Cash received on allotment ₹2,75,200; Balance of Share Forfeiture A/c ₹1,000; Capital Reserve ₹3,000; Balance of Securities Premium Reserve A/c ₹3,96,600; Total of Balance Sheet ₹13,97,600.]

Hints : (*i*) Securities Premium Reserve A/c will be debited in the entry of forfeiture.

(*ii*) Amount transferred to Capital Reserve :

		₹
Profit on 800 shares of Y	=	2,400

Profit on 600 shares of $X = \frac{₹3,000}{900 \text{ Shares}} \times 600$ Shares = 2,000

4,400

Less : Loss on re-issue of 1,400 shares @ ₹1 each 1,400

3,000

Q. 96. *X* Ltd. issued 50,000 shares of ₹10 each at a premium of ₹2 per share payable as follows :

₹3 on Application
₹6 on Allotment (including premium) and
₹3 on call.

Applications were received for 75,000 shares and pro-rata allotment was made as follows :

To the applicants of 40,000 shares, 30,000 shares were issued and for the rest 20,000 shares were issued. All moneys due were received except the allotment and call money from Ram who had applied for 1,200 shares (out of the group of 40,000 shares). All his shares were forfeited. The forfeited shares were re-issued for ₹7 per share fully paid-up.

Pass necessary journal entries for the above transactions.

[Ans. Amount received on allotment ₹2,20,500; Amount received on first & final call ₹1,47,300; Amount transferred to Capital Reserve ₹900.]

Hint. Scheme of Allotment :

	Applied		*Allotted*	
	40,000	Shares	30,000	Shares
Remaining	35,000	Shares	20,000	Shares
	75,000		50,000	

Q. 97. Shiva Ltd. invited applications for issuing 2,00,000 Equity Shares of ₹100 each at a premium of ₹60 per share. The amount was payable as follows :

On application ₹30 per share (including premium ₹10).

On allotment ₹70 per share (including premium ₹50).

On first and final call the balance amount.

Applications for 1,90,000 shares were received. Shares were allotted to all the applicants and the company received all money due on allotment except Jain who had been allotted 1,000 shares, and his shares were immediately forfeited. Afterwards first and final call was made. Gupta did not pay the first and final call on his 2,000 allotted shares. His shares were also forfeited. 50% of the forfeited shares of both Jain and Gupta were re-issued for ₹90 per share fully paid up.

Pass necessary journal entries in the books of Shiva Ltd. for the above transactions.

[Ans. Amount received on Allotment ₹1,32,30,000. Amount received on first and final call ₹1,12,20,000; Forfeiture amount ₹20,000 + ₹80,000; Capital Reserve ₹35,000.]

Hint. Securities Premium Reserve A/c will be debited from ₹50,000 at the time of forfeiture of 1,000 shares and it will not be debited at the time of forfeiture of 2,000 shares.

Q. 98. *X* Ltd. issued 40,000 Equity Shares of ₹10 each at a premium of ₹2.50 per share. The amount was payable as follows :

On Application	₹2 per share
On Allotment	₹4.50 per share (including premium)
On Call	₹6 per share

Owing to heavy subscription the allotment was made on pro-rata basis as follows:

(*a*) Applicants for 20,000 shares were allotted 10,000 shares.

(*b*) Applicants for 56,000 shares were allotted 14,000 shares.

(*c*) Applicants for 48,000 shares were allotted 16,000 shares.

It was decided that excess amount received on applications would be utilised on allotment and the surplus would be refunded.

Ram, to whom 1,000 shares were allotted, who belong to cateogry (*a*), failed to pay allotment money. His shares were forfeited after the call.

Pass the necessary Journal entries in the books of *X* Ltd. for the above transactions.

[**Ans.** Amount received on Allotment ₹30,500; Amount received on First & Final Call ₹2,34,000; Forfeited Shares Account ₹4,000]

LATEST EXAMINATION QUESTIONS

Q. 1. Saturn Ltd. was registered with an authorized capital of ₹12,00,000, divided into 1,20,000 equity shares of ₹10 each. It issued 40,000 equity shares to the public at a premium of ₹5 per share, payable as follows :

On application	₹6
On allotment	₹9 (including premium of ₹5)

All the shares were applied for and allotted. One shareholder holding 500 shares did not pay the allotment money and his shares were forfeited. Out of the forfeited shares, the company reissued 400 shares at ₹7 per share fully called up.

You are required to :

(*a*) Pass journal entries in the books of the company.

(*b*) Prepare :

(*i*) Securities Premium Reserve Account, and

(*ii*) Share Capital Account. *(I.S.C. 2018)*

SOLUTION : JOURNAL OF ABC LTD.

Date	*Particulars*		*L.F.*	*Dr.* (₹)	*Cr.* (₹)
	Bank A/c	Dr.		2,40,000	
	To Share Application A/c				2,40,000
	(Share application money received)				
	Share Application A/c	Dr.		2,40,000	
	To Equity Share Capital A/c				2,40,000
	(Share application transferred to Share Capital A/c)				

	Share Allotment A/c Dr.		3,60,000	
	To Equity Share Capital A/c			1,60,000
	To Securities Premium Reserve A/c			2,00,000
	(Share allotment due)			
	Bank A/c Dr.		3,55,500	
	Calls-in-Arrears A/c Dr.		4,500	
	To Share Allotment A/c			3,60,000
	(Share allotment received)			
	Equity Share Capital A/c Dr.		5,000	
	Securities Premium Reserve A/c Dr.		2,500	
	To Share Forfeiture A/c			3,000
	To Calls-in-Arrears A/c			4,500
	(500 shares forfeited)			
	Bank A/c Dr.		2,800	
	Share Forfeiture A/c Dr.		1,200	
	To Equity Share Capital A/c			4,000
	(400 shares reissued)			
	Share Forfeiture A/c Dr.		1,200	
	To Capital Reserve A/c(1)			1,200
	(Gain on reissued shares transferred to capital reserve)			

Dr. SECURITIES PREMIUM RESERVE ACCOUNT Cr.

Particulars	₹	*Particulars*	₹
To Calls-in-Arrear A/c	2,500	By Share Allotment A/c	2,00,000
To Balance c/d	1,97,500		
	2,00,000		2,00,000

Dr. SHARE CAPITAL ACCOUNT Cr.

Particulars	₹	*Particulars*	₹
To Share Forfeiture A/c	3,000	By Share Application A/c	2,40,000
To Calls-in-arrears A/c	2,000	By Share Allotment A/c	1,60,000
To Balance c/d	3,99,000	By Bank A/c	2,800
		By Share Forfeiture A/c	1,200
	4,04,000		4,04,000

Note (1)

		₹
Forfeited amount on 500 shares	= 3,000	
Hence, Forfeited amount on 400 shares	$= \frac{3,000}{500} \times 400 =$	2,400
Less : Loss on Reissue		1,200
Amount transferred to Capital Reserve		1,200

Q. 2. Meera Ltd. invited applications for 50,000 equity shares of ₹10 each at a premium of ₹2 per share, payable as follows :

On Application on 1st May, 2017	₹2	
On Allotment on 1st July, 2017	₹5	(including premium)
On 1st and Final Call on 1st October, 2017	₹5	

The Company received applications for 62,500 shares.

It was decided to :

(*a*) Refuse allotment to the applicants of 2,500 shares.

(*b*) Allot in full to applicants of 10,000 shares.

(*c*) Allot the balance of the shares applied on a pro-rata basis among the other applicants.

(*d*) Utilize the excess application money in part payment of allotment money.

(*e*) Charge interest on calls-in-arrears, if any, @ 10% per annum.

All the money due was received except from one shareholder to whom 200 shares had been allotted in full. The amount was due by him to the company even till the date of the Balance Sheet, which was 31st March, 2018.

The company charged interest on calls-in-arrears from the shareholder from the date on which it was due till the Balance Sheet date.

You are required to, for the the year 2017-18 :

(*i*) Prepare the Cash Book to record the above issue of shares.

(*ii*) Pass journal entries in the Journal Proper (including entries for interest on calls-in-arrears). *(I.S.C. 2019)*

SOLUTION :

Dr. CASH BOOK (BANK COLUMN) Cr.

Receipts	*Amount*	*Payments*	*Amount*
	₹		₹
To Equity Share Application A/c	1,25,000	By Equity Share Application A/c	5,000
To Equity Share Allotment A/c	2,29,000	By Balance c/d	5,98,000
To Equity Share 1st & Final Call A/c	2,49,000		
	6,03,000		6,03,000

JOURNAL OF MEERA LTD.

Date	*Particulars*		*L.F.*	*Dr.*	*Cr.*
				₹	₹
	Equity Share Application A/c	Dr.		1,20,000	
	To Equity Share Capital A/c				1,00,000
	To Equity Share Allotment A/c				20,000
	(Share Application transferred to share capital)				
	Equity Share Allotment A/c	Dr.		2,50,000	
	To Equity Share Capital A/c				1,50,000
	To Securities Premium Reserve A/c				1,00,000
	(Share allotment due)				

	Calls-in-arrears A/c Dr. To Equity Share Allotment A/c (Amount not received on allotment)		1,000	1,000
	Equity Share 1st & Final Call A/c Dr. To Equity Share Capital A/c (1st & Final call due)		2,50,000	2,50,000
	Calls-in-arrears A/c Dr. To Equity Share 1st & Final Call A/c (Amount not received on 1st & final call)		1,000	1,000
	Shareholders A/c Dr. To Interest on calls-in-arrears A/c (Interest on calls in arrears due from shareholder)		125	125
	Interest on calls-in-arrears A/c Dr. To Statement of Profit & Loss (Interest on calls in arrears account closed)		125	125

Working Note :

	₹
Interest on ₹1,000 @ 10% p.a. from 1st July 2017 to 31st March, 2018 :	75
Interest on ₹1,000 @ 10% p.a. from 1st Oct. 2017 to 31st March, 2018	50
	125

Q. 3. Sudesh Ltd. was registered with an authorised capital of ₹40,00,000 divided into 4,00,000 Equity Shares of ₹10 each.

The company offered 50,000 shares to the public at a premium of ₹2 per share, payable as follows :

₹3 on application

₹6 on allotment (including premium)

₹3 on first and final call (due two months after allotment)

Applications were received for 60,000 shares and pro-rata allotment was made as follows :

Category A : The applicants of 40,000 shares were allotted 30,000 shares.

Category B : The applicants of 20,000 shares were allotted in full.

Excess money paid on application was utilized towards allotment.

Nobby, a shareholder from Category A, who had applied for 1,200 shares failed to pay the allotment and call money.

Vineet, a shareholder from Category B, who had been allotted 1,000 shares, paid the call money due, along with allotment.

The company forfeited Nobby's shares after the first and final call and paid interest on Calls-in-advance to Vineet @ 12% per annum on the day of the final call.

You are required to :

(*i*) Pass journal entries to record the above transactions in the books of the company (including entries for interest on Calls-in-advance).

(*ii*) Prepare Calls-in-arrears Account. *(I.S.C. 2020)*

SOLUTION :

Sudesh Ltd.

JOURNAL

Date	*Particulars*		*L.F.*	*Dr. Amount* ₹	*Cr. Amount* ₹
	Bank A/c	Dr.		1,80,000	
	To Share Application A/c				1,80,000
	(Application money received)				
	Share Application A/c	Dr		1,80,000	
	To Share Capital A/c				1,50,000
	To Share Allotment A/c				30,000
	(Application money transferred)				
	Share Allotment A/c	Dr.		3,00,000	
	To Share Capital A/c				2,00,000
	To Securities Premium Reserve A/c				1,00,000
	(Allotment money due on 50,000 equity shares @ ₹6 each)				
	Bank A/c[(2)]	Dr.		2,68,500	
	Calls in Arrears A/c	Dr.		4,500	
	To Share Allotment A/c				2,70,000
	To Calls in Advance A/c				3,000
	(Allotment money and Calls in Advance received)				
	Share First and Final Call A/c	Dr.		1,50,000	
	To Share Capital A/c				1,50,000
	(First and Final Call money due on 50,000 equity shares @ ₹3 each)				
	Bank A/c	Dr.		1,44,300	
	Calls in Arrears A/c	Dr.		2,700	
	Calls in Advance A/c	Dr.		3,000	
	To Share First and Final Call A/c				1,50,000
	(First and Final call money received)				
	Share Capital A/c	Dr.		9,000	
	Securities Premium Reserve A/c	Dr.		1,800	
	To Calls in Arrears A/c				7,200
	To Share Forfeiture A/c				3,600
	(900 Shares forfeited)				
	Interest on Calls-in-Advance A/c[(3)]	Dr.		60	
	To Sundry Members A/c				60
	(Interest due on Calls-in-Advance)				
	Sundry Members A/c	Dr.		60	
	To Bank A/c				60
	(Interest paid on Calls-in-Advance)				
	Statement of Profit & Loss	Dr.		60	
	To Interest on Calls-in-Advance A/c				60
	(Interest on Calls in advance transferred to Statement of Profit & Loss)				

Dr. **CALLS IN ARREARS ACCOUNT** Cr.

Particulars	₹	*Particulars*	₹
To Share Allotment A/c	4,500	By Share Capital A/c	5,400
To Share First & Final Call A/c	2,700	By Securities Premium Reserve A/c	1,800
	7,200		7,200

Working Note :

(1) Shares allotted to Nobby : $1,200 \times \frac{30,000}{40,000} = 900$

Excess application money received from Nobby :

$(1,200 - 900) \times 3 = 900$

	₹
Amount due on allotment from Nobby = 900 × ₹6	5,400
Less : Excess received on application	900
Amount not received from Nobby on allotment	4,500

(2)

Total amount due on allotment : 50,000 × ₹6	3,00,000
Less : Excess received on allotment	30,000
	2,70,000
Less : Not received on allotment	4,500
	2,65,500
Add : Calls Received in Advance	3,000
	2,68,500

(3) Interest on Calls in Advance :

$$3,000 \times \frac{12}{100} \times \frac{2}{12} = ₹60$$

MULTIPLE CHOICE QUESTIONS

Select the Best Alternate and tally your answer with the Answers given at the end of the book :

(i) Meaning and Characteristics of a Company

Q. 1. A company has ....

(A) Separate Legal Entity (B) Perpetual Existence

(C) Limited Liability (D) All of the Above

Q. 2. Shareholders are :

(A) Customers of the Company (B) Owners of the Company

(C) Creditors of the Company (D) None of these

Q. 3. Who are the real owners of a company?

(A) Government (B) Board of Directors

(C) Equity shareholders (D) Debentureholders

Q. 4. A Company is created by :

(A) Special act of the Parliament (B) Companies Act

(C) Investors (D) Members

Q. 5. An artificial person created by Law is called :

(A) Sole Tradership
(B) Partnership Firm
(C) Company
(D) All of the Above

Q. 6. The liability of members in a Company is :

(A) Limited
(B) Unlimited
(C) Stable
(D) Fluctuating

Q. 7. Liability of a shareholder is limited to .... of the shares allotted to him.

(A) Paid up Value
(B) Called up value
(C) Face value
(D) Reserve Price

Q. 8. Maximum number of members in a private company is :

(A) 7
(B) 200
(C) 20
(D) No Limit

(ii) Meaning, Nature and Types of Shares

Q. 9. Capital of a Company is divided in units which is called :

(A) Debenture
(B) Share
(C) Stock
(D) Bond

Q. 10. Shareholders receive from the company :

(A) Interest
(B) Commission
(C) Profit
(D) Dividend

Q. 11. Equity shares cannot be issued for the purpose of :

(A) Cash Receipts
(B) Purchase of assets
(C) Redemption of debentures
(D) Distribution of dividend

Q. 12. A Company may issue ....

(A) Equity Shares
(B) Preference Shares
(C) Equity and Preference both shares
(D) None of the Above

HOTS

Q. 13. A company cannot issue :

(A) Redeemable Equity Shares
(B) Redeemable Preference Shares
(C) Redeemable Debentures
(D) Fully Convertible Debentures

Q. 14. To whom dividend is given at a fixed rate in a company?

(A) To equity shareholders
(B) To preference shareholders
(C) To debentureholders
(D) To promoters

Q. 15. Preference shareholders have

(A) Preferential right as to dividend only
(B) Preferential right in the management
(C) Preferential right as to repayment of capital at the time of liquidation of the company
(D) Preferential right as to dividend and repayment of capital at the time of liquidation of the company

Q. 16. The shares on which there is no any pre-fixed rate of dividend is decided, but the rate of dividend is fluctuating every year according to the availability of profits, such share are called :

(A) Equity Share
(B) Non-cumulative preference share
(C) Non-convertible preference share
(D) Non-guaranteed preference share

Q. 17. Preference shares, in case the holders of these have a right to convert their preference shares into equity shares at their option according to the terms of issue, such shares are called :

(A) Cumulative Preference Share
(B) Non-cumulative Preference Share
(C) Convertible Preference Share
(D) Non-convertible Preference Share

Q. 18. A preference share which does not carry the right of sharing in surplus profits is called ....

(A) Non-Cumulative Preference Share

(B) Non-participating Preference Share

(C) Irredeemable Preference Share

(D) Non-convertible Preference Share

Q. 19. Which shareholders have a right to receive the arrears of dividend from future profits :

(A) Redeemable Preference Shares
(B) Participating Preference Shares
(C) Cumulative Preference Shares
(D) Non-Cumulative Preference Shares

Q. 20. Which shareholders are returned their capital after some specified time :

(A) Redeemable Preference Shares
(B) Irredeemable Preference Shares
(C) Cumulative Preference Shares
(D) Participating Preference Shares

HOTS

Q. 21. The following statements apply to equity/preference shareholders. Which one of them applies only to preference shareholders?

(A) Shareholders risk the loss of investment
(B) Shareholders bear the risk of no dividends in the event of losses
(C) Shareholders usually have the right to vote
(D) Dividends are usually given at a set amount in every financial year.

HOTS

Q. 22. Unless otherwise stated, a preference share is always deemed to be :

(A) Cumulative, participating and non-convertible
(B) Non-cumulative, non-participating and non-convertible
(C) Cumulative, non-participating and non-convertible
(D) Non-cumulative, participating and non-convertible

(iii) Meaning, Nature and Types of Share Capital

Q. 23. Nominal Share Capital is ....

(A) that part of authorised capital which is issued by the company

(B) the amount of capital which is actually applied by the prospective shareholders

(C) the amount of capital which is actually paid by the shareholders

(D) the maximum amount of share capital which a company is authorised to issue *(C.B.S.E. 2020, Kolkata, Lucknow)*

Q. 24. Subscribed capital is :

(A) That part of authorised capital which is issued to the public for subscription.

(B) That part of issued capital which has been actually subscribed by the public.

(C) That part of subscribed capital which has been called up on the shares.

(D) That part of subscribed capital which has not yet been called up on the shares. *(C.B.S.E. 2020, Rajasthan)*

Q. 25. Krishan Ltd. has Issued Capital of 20,00,000 Equity shares of ₹10 each. Till Date ₹8 per share have been called up and the entire amount received except calls of ₹4 per share on 800 shares and ₹3 per share from another holder who held 500 shares. What will be amount appearing as 'Subscribed but not fully paid capital' in the balance sheet of the company?

(A) ₹ 5,700 (B) ₹1,95,99,000

(C) ₹1,59,95,300 (D) ₹1,99,95,300

(C.B.S.E. Sample Paper, 2021)

Q. 26. The portion of the capital which can be called-up only on the winding up of the Company is called.................. .

(A) Authorised Capital (B) Called up Capital

(C) Uncalled Capital (D) Reserve Capital

Q. 27. Capital included in the Total of Balance Sheet of a Company is called :

(A) Issued Capital (B) Subscribed Capital

(C) Called up Capital (D) Authorised Capital

Q. 28. .... is transferred to Capital Reserve.

(A) Gain from sale of fixed assets

(B) Gain on purchase of running business

(C) Gain on reissue of forfeiture of shares

(D) All of the Above

Q. 29. Reserve Capital is also known by :

(A) Capital Reserve (B) Called up Capital

(C) Subscribed Capital (D) None of the above

Q. 30. Reserve Capital is :

(A) Subscribed Capital
(B) Capital Reserve
(C) Uncalled Capital
(D) Part of the uncalled capital which may be called only at the time of liquidation of the Company.

Q. 31. Which of the following statements does not relate to 'Reserve Capital':

(A) It is part of uncalled capital of a company.
(B) It cannot be used during the lifetime of a company.
(C) It can be used for writing off capital losses.
(D) It is part of subscribed capital. *(C.B.S.E. 2020, Mumbai, Chennai)*

Q. 32. In the Balance Sheet of a company, under the heading share capital, at the last is shown :

(A) Authorised Share Capital (B) Subscribed Share Capital
(C) Issued Share Capital (D) Reserve Share Capital

Q. 33. Which of the following is not shown under the heading 'Share Capital' in a Balance Sheet :

(A) Subscribed Capital (B) Issued Capital
(C) Reserve Capital (D) Authorised Capital

Q. 34. Reserve Capital is a part of :

(A) Paid-up Capital
(B) Forfeited Share Capital
(C) Assets
(D) Capital to be called up only on liquidation of company

HOTS

Q. 35. Which of the following statement is/are true?

(*i*) Authorized Capital < Issued Capital
(*ii*) Authorized Capital ≥ Issued Capital
(*iii*) Subscribed Capital ≤ Issued Capital
(*iv*) Subscribed Capital > Issued Capital

(A) (*i*) only (B) (*i*) and (*iv*) Both
(C) (*ii*) and (*iii*) Both (D) (*ii*) only

(C.B.S.E. Sample Paper, 2021)

Q. 36. Authorised Capital of a Company is mentioned in :

(A) Memorandum of Association (B) Articles of Association
(C) Prospectus (D) Statement in lieu of Prospectus

Q. 37. In case of private placement of shares, the lock in period is :

(A) 1 Year (B) 2 Years
(C) 3 Years (D) None of the above

Q. 38. In case of private placement of shares and company does not invite the general public for subscription of shares in that case, company instead of issuing prospectus :

(A) Prepares the statement in lieu of prospectus
(B) Prepares the Report
(C) Prepares the Budget
(D) Prepares the Asset side of Balance Sheet

Q. 39. In case of private placement of shares, to raise the amount of capital a company :
(A) invites the public through prospectus
(B) does not invite the public
(C) invites the public through advertisement
(D) invites the public through memorandum of association

Q. 40. Shares issued by a company to its employees or directors in consideration of 'Intellectual Property Rights' are called :
(A) Right Equity Shares (B) Private Equity Shares
(C) Sweat Equity Shares (D) Bonus Equity Shares

(iv) Issue and Allotment of Shares

Q. 41. A Company may issue the shares :
(A) By Private Placement of Shares
(B) By Public Subscription of Shares
(C) For Consideration other than cash
(D) By All of the Above

Q. 42. Public subscription of shares include :
(A) To Issue Prospectus (B) To Receive Applications
(C) To Make Allotment (D) All of the Above

Q. 43. Which of the following will define, when appropriation of a certain number of shares is made to an applicant in response to his application?
(A) Share allotment (B) Share forfeiture
(C) Share trading (D) Share Purchase

Q. 44. Issue of shares at a price lower than its face value is called :
(A) Issue at a Loss (B) Issue at a Profit
(C) Issue at a Discount (D) Issue at a Premium

Q. 45. According to SEBI Guidelines, Minimum Subscription has been fixed at .... of the issued amount.
(A) 25% (B) 50%
(C) 90% (D) 100%

Q. 46. One of the conditions, in addition to others, for allotment of shares is :
(A) Resolution in General Meeting (B) Receiving Minimum Subscription
(C) Full Subscription by Public (D) Full Payment on Application

Q. 47. Persons who start a company are called ....
(A) Shareholders (B) Directors
(C) Promoters (D) Auditors

Q. 48. Minimum subscription amount of 90% is related to which share capital :

(A) Authorised Capital (B) Issued Capital
(C) Paid up Capital (D) Reserve Capital

Q. 49. Share Application Account is in the nature of :

(A) Real Account (B) Personal Account
(C) Nominal Account (D) None of the above

Q. 50. As per SEBI Guidelines, Application money should not be less than .... of the issue price of each share.

(A) 10% (B) 15%
(C) 25% (D) 50%

Q. 51. 4,000 Equity Shares of ₹10 each were issued at 8% premium to the promoters of a company for their services. Which account will be debited?

(A) Share Capital Account
(B) Goodwill Account/Incorporation Cost Account
(C) Securities Premium Reserve Account
(D) Cash Account

Q. 52. Excess value of net assets over purchase consideration at the time of purchase of business is :

(A) Credited to the Capital Reserve.
(B) Debited to the Goodwill Account.
(C) Credited to the General Reserve Account.
(D) Credited to the Vendor's Account. *(C.B.S.E. 2020, Rajasthan)*

Q. 53. If vendors are issued fully paid shares of ₹1,25,000 in consideration of net assets of ₹1,50,000, the balance of ₹25,000 will be credited to :

(A) Statement of Profit & Loss (B) Goodwill Account
(C) Security Premium Reserve Account (D) Capital Reserve Account

Q. 54. Issue of shares at a price higher than its face value is called :

(A) Issue at a Profit (B) Issue at a Premium
(C) Issue at a Discount (D) Issue at a Loss

Q. 55. On issue of shares Premium is :

(A) Profit (B) Income
(C) Revenue Receipt (D) Capital Profit

Q. 56. Newfound Ltd. took over business of Old Land Ltd. and paid for it by issue of 30,000 Equity Shares of ₹100 each at par along with 6% Preference Shares of ₹1,00,00,000 at a premium of 5% and a cheque of ₹8,00,000. What was the total agreed purchase consideration payable to Old Land Ltd.

(A) ₹1,05,00,000 (B) ₹1,43,00,000
(C) ₹1,40,00,000 (D) ₹1,35,00,000

(C.B.S.E. Sample Paper, 2021)

Q. 57. In which of the following situation Companies Act 2013 allows for issue of shares at discount?

(A) Issued to vendors (B) Issued to public
(C) Issued as sweat equity (D) None of the above
(C.B.S.E. Sample Paper, 2021)

Q. 58. As per Section 52 of Companies Act 2013, Securities Premium Reserve cannot be utilised for :
(A) Writing off capital losses
(B) Issue of fully paid bonus shares
(C) Writing off discount on issue of securities
(D) Writing off preliminary expenses *(C.B.S.E. Sample Paper, 2021)*

Q. 59. Net Assets minus Capital Reserve is :
(A) Purchase consideration (B) Goodwill
(C) Total assets (D) Liquid assets
(C.B.S.E. Sample Paper, 2021)

HOTS

Q. 60. Which of the following is not a capital profit?
(A) Profit prior to incorporation of the company
(B) Profit from the sale of fixed assets
(C) Premium on issue of shares
(D) Compensation received on the termination of a contract

Q. 61. Maximum limit of Premium on shares is:
(A) 5% (B) 10%
(C) No Limit (D) 100%

Q. 62. When a company issues shares at a premium, the amount of premium should be received by the company :
(A) Along with application money (B) Along with allotment money
(C) Along with calls (D) Along with any of the above

Q. 63. Amount of securities premium can be utilised for :
(A) Writing off the preliminary expenses of the company
(B) Issuing bonus shares to the shareholders of the company
(C) Buy-back of its own shares
(D) All of the above

Q. 64. For what purpose securities premium reserve account cannot be utilized?
(A) Amortization of preliminary expenses
(B) Distribution of dividend
(C) Issue of fully paid bonus shares
(D) Buy Back of own shares

Q. 65. Which of the following is not a purpose for which the Securities Premium amount can be used?
(A) Issuing fully paid bonus shares to shareholders.
(B) Issuing partly paid up bonus shares to shareholders.
(C) Writing off preliminary expenses of the company.
(D) In purchasing its own shares (buy back) *(C.B.S.E. 2020, Punjab)*

Q. 66. Premium on the issue of shares should be shown :

(A) On the Assets side of balance sheet
(B) On the Equity & Liabilities side of balance sheet
(C) In profit & loss Statement
(D) None of the Above

Q. 67. A Company issued 50,000 shares of ₹20 each at 5% premium. ₹10 were payable on application and balance on allotment. What will be the allotment amount?

(A) ₹5,00,000 (B) ₹4,75,000
(C) ₹5,50,000 (D) ₹5,25,000

Q. 68. Interest on calls in arrears is charged according to Table F at :

(A) 6% p.a. (B) 10% p.a.
(C) 5% p.a. (D) 12% p.a.

Q. 69. Amount of Calls in Arrears is shown in the Balance Sheet

(A) as deduction from issued capital
(B) as deduction from subscribed capital
(C) as addition to subscribed capital
(D) on the assets side

Q. 70. As per Table F, the Company is required to pay .... interest on the amount of calls in advance.

(A) 12% p.a. (B) 5% p.a.
(C) 10% p.a. (D) 6% p.a.

Q. 71. Amount of Calls in Advance is

(A) Added to Share Capital
(B) Deducted from Share Capital
(C) Shown on the Assets side
(D) Shown on the Equity & Liabilities side

Q. 72. First call amount received in advance from the shareholders before it is actually called up by the directors is :

(A) Debited to calls-in-advance account.
(B) Credited to share allotment account.
(C) Debited to first call account.
(D) Credited to calls-in-advance account. *(C.B.S.E. 2020, Rajasthan)*

HOTS

Q. 73. Following amounts were payable on issue of shares by a Company : ₹3 on application, ₹3 on allotment, ₹2 on first call and ₹2 on final call. *X* holding 500 shares paid only application and allotment money whereas *Y* holding 400 shares did not pay final call. Amount of calls in arrear will be :

(A) ₹3,800 (B) ₹2,800
(C) ₹1,800 (D) ₹6,200

Q. 74. The subscribed capital of a company is ₹80,00,000 and the nominal value of the share is ₹100 each. There were no calls in arrear till the final call was made. The final call made was paid on 77,500 shares only. The balance in the calls in arrear amounted to ₹62,500. Calculate the final call on share.

(A) ₹ 7 (B) ₹20

(C) ₹22 (D) ₹25

Q. 75. A shareholder holding 600 shares paid the amount of call @ ₹5 per share on 1st November 2018 whereas the call was due on 1st March 2019. Interest on calls in advance as per Table F will be :

(A) ₹45 (B) ₹ 60

(C) ₹50 (D) ₹120

Q. 76. From which account, expenses on issue of shares will be written off first of all :

(A) Statement of Profit and Loss

(B) Miscellaneous Expenditure Account

(C) Share Issue Expenses Account

(D) Securities Premium Reserve Account

Q. 77. Pro-rata allotment of shares is made when there is :

(A) Under subscription (B) Oversubscription

(C) Equal subscription (D) As and when desired by directors

Q. 78. Authorised capital of a Company is divided into 5,00,000 shares of ₹10 each. It issued 3,00,000 shares. Public applied for 3,60,000 shares. Amount of issued capital will be :

(A) ₹30,00,000 (B) ₹36,00,000

(C) ₹50,00,000 (D) ₹ 6,00,000

Q. 79. A Company invited applications for 1,00,000 shares and it received applications for 1,50,000 shares. Applications for 30,000 shares were rejected and the remaining were allotted shares on prorata basis. How many shares an applicant for 3,000 shares will be allotted?

(A) 2,500 Shares (B) 3,600 Shares

(C) 4,500 Shares (D) 2,000 Shares

HOTS

Q. 80. *E* Ltd. had allotted 10,000 shares to the applicants of 14,000 shares on pro-rata basis. The amount payable on application was ₹2. *F* applied for 420 shares. The number of shares allotted and the amount carried forward for adjustment against allotment money due from *F* will be :

(A) 60 shares; ₹120 (B) 340 shares; ₹160

(C) 320 shares, ₹200 (D) 300 shares; ₹240

Q. 81. Anish Ltd. issued a prospectus inviting applications for 2,000 shares. Applications were received for 3,000 shares and pro-rata allotment was made to the applicants of 2,400 shares. If Dhruv has been allotted 40 shares, how many shares he must have applied for?

(A) 40 (B) 44

(C) 48 (D) 52

(C.B.S.E. Sample Paper, 2021)

Q. 82. A Company offered 50,000 shares of ₹10 each at par payable as to ₹3 on applications, ₹5 on allotment and the balance on final call. Applications were received for 60,000 shares and the allotment was made pro-rata. The excess application money was to be adjusted on allotment and call. How much amount will be transferred from Share Application A/c to Share Allotment A/c?

(A) ₹1,80,000 (B) ₹30,000
(C) ₹1,50,000 (D) ₹50,000

HOTS

Q. 83. A company issued 4,000 equity shares of ₹10 each at par payable as under : On application ₹3; on allotment ₹2; on first call ₹4 and on final call ₹1 per share.

Applications were received for 13,000 shares. Applications for 3,000 shares were rejected and pro-rata allotment was made to the applicants for 10,000 shares. How much amount will be received in cash on first call? Excess application money is adjusted towards amount due on allotment and calls.

(A) ₹ 6,000 (B) Nil
(C) ₹16,000 (D) ₹10,000

HOTS

Q. 84. A company issued 4,000 equity shares of ₹10 each at par payable as under : On application ₹3; on allotment ₹2; on first call ₹4 and on final call ₹1 per share.

Applications were received for 10,000 shares. Allotment was made pro-rata. How much amount will be received in cash on allotment?

(A) ₹8,000 (B) ₹12,000
(C) Nil (D) None

HOTS

Q. 85. A company issued 5,000 equity shares of ₹100 each at par payable as to : ₹40 on application; ₹50 on allotment and ₹10 on call.

Applications were received for 8,000 shares. Allotment was made on pro-rata. How much amount will be received in cash on allotment?

(A) ₹2,50,000 (B) ₹1,20,000
(C) ₹1,30,000 (D) ₹ 50,000

Q. 86. A Company purchased a building for ₹3,60,000 and issued as payment equity shares at 20% premium. Journal Entry will be :

(A) Building A/c	Dr.	4,00,000	
To Share Capital A/c			3,20,000
To Securities Premium Reserve A/c			80,000

(B) Share Capital A/c	Dr.	4,00,000	
To Building A/c			3,60,000
To Securities Premium Reserve A/c			40,000

(C) Building A/c	Dr.	3,60,000	
To Share Capital A/c			3,00,000
To Securities Premium Reserve A/c			60,000

(D) Building A/c	Dr.	3,60,000	
To Share Capital A/c			60,000
To Securities Premium Reserve A/c			3,00,000

Q. 87. A Company purchased a Building for ₹12,00,000 out of which ₹2,00,000 were paid in cash. Balance amount was paid by issue of equity shares of ₹10 each at 25% premium. How many shares will be issued by the Company?

(A) 1,00,000 Shares
(B) 80,000 Shares
(C) 1,20,000 Shares
(D) 96,000 Shares

Q. 88. If shares of ₹4,00,000 are issued for purchase of assets of ₹5,00,000, ₹1,00,000 will be treated as ....

(A) Discount
(B) Premium
(C) Profit
(D) Loss

Q. 89. A Building was purchased for ₹9,00,000 and payment was made in ₹100 shares at 20% premium. Securities Premium Reserve A/c will be ....

(A) Debited by ₹1,50,000
(B) Credited by ₹1,50,000
(C) Debited by ₹1,80,000
(D) Credited by ₹1,80,000

Q. 90. A company purchased machinery for ₹1,80,000 and in consideration issued shares at 20% premium. What will be the face value of shares issued :

(A) ₹1,50,000
(B) ₹1,44,000
(C) ₹1,80,000
(D) ₹2,16,000

(v) Forfeiture of Shares

Q. 91. Forfeiture of shares results in the reduction of :

(A) Subscribed Capital
(B) Authorised Capital
(C) Reserve Capital
(D) Fixed Assets

Q. 92. Which one of the following items is not a part of subscribed capital?

(A) Equity Shares
(B) Preference Shares
(C) Forfeited Shares
(D) Bonus Shares

Q. 93. At the time of forfeiture of shares the share capital account is debited with

(A) Face value
(B) Called up value
(C) Paid up value
(D) Issued value

Q. 94. Voluntary return of shares for cancellation by the shareholders is called

(A) Cancellation of shares
(B) Forfeiture
(C) Surrender of shares
(D) None of these

Q. 95. If the Premium on the forfeited shares has already been received, then Securities Premium A/c should be :

(A) Credited
(B) Debited
(C) No treatment
(D) None of these

HOTS

Q. 96. Balance of share forfeiture account is shown in the balance sheet under the head ....

(A) Share Capital Account (B) Reserve and Surplus
(C) Current Liabilities and Provisions (D) Unsecured Loans

Q. 97. On an equity share of ₹10 the company has called up ₹8 but ₹6 have been received by the company is forfeited, the capital account should be debited by:

(A) ₹10 (B) ₹ 8
(C) ₹ 6 (D) ₹ 2

Q. 98. If a share of ₹10 issued at a premium of ₹3 on which the full amount has been called and ₹8 (including premium) paid is forfeited the capital account should be debited with :

(A) ₹ 5 (B) ₹ 8
(C) ₹10 (D) ₹13

Q. 99. If a share of ₹10 issued at a premium of ₹1 on which ₹ 9 (including premium) have been called and ₹7 including premium is paid is forfeited, the capital account should be debited by :

(A) ₹10 (B) ₹ 7
(C) ₹ 8 (D) ₹ 9

Q. 100. 600 shares of ₹10 each were forfeited for non-payment of ₹2 per share on first call and ₹5 per share on final call. Share Forfeiture Account will be credited with :

(A) ₹1,200 (B) ₹1,800
(C) ₹3,000 (D) ₹4,200

Q. 101. 800 shares of ₹10 each issued at 20% premium were forfeited for non-payment of allotment money of ₹5 (including premium) and first & final of ₹3 per share. Share Forfeiture Account will be credited with :

(A) ₹1,600 (B) ₹2,400
(C) ₹3,200 (D) ₹4,800

Q. 102. 800 shares of ₹10 each issued at 30% premium (to be paid on allotment) were forfeited for non-payment of ₹2 per share on first call and ₹2 per share on final call. Share Forfeiture Account will be credited with :

(A) ₹2,400 (B) ₹4,800
(C) ₹3,200 (D) ₹7,200

Q. 103. A Company forfeited 300 shares of ₹10 each, ₹8 per share called up, on which *Y* had paid application and allotment money of ₹6 per share. Share Forfeiture Account will be credited with :

(A) ₹ 600 (B) ₹1,800
(C) ₹1,200 (D) ₹2,400

Q. 104. On 300 equity shares of ₹10 the company has called up ₹8 but ₹6 have been received by the company are forfeited, the forfeiture account should be credited by :

(A) ₹2,400 (B) ₹1,200
(C) ₹1,800 (D) ₹ 600

Q. 105. If 400 shares of ₹10 issued at a premium of ₹3 on which the full amount has been called and ₹8 (including premium) have been received are forfeited, the forfeiture account should be credited with :

(A) ₹3,200 (B) ₹2,000
(C) ₹1,200 (D) ₹2,800

Q. 106. If 500 shares of ₹10 issued at a premium of ₹1 on which ₹9 (including premium) have been called and ₹7 including premium have been paid are forfeited, the forfeiture account should be credited by :

(A) ₹3,000 (B) ₹3,500
(C) ₹4,000 (D) ₹4,500

Q. 107. Mohit had been allotted 600 shares by Govinda Ltd. on pro rata basis which had issued two shares for every three applied. He had paid application money of ₹3 per share and could not pay allotment money of ₹5 per share. First and final call of ₹2 per share was not yet made by the company. His shares were forfeited. The following entry will be passed:

Equity Share Capital A/c	Dr.	₹X	
To Shares Forfeited A/c			₹Y
To Equity Share Allotment A/c			₹Z

Here *X*, *Y* and *Z* are :

(A) ₹6,000; ₹2,700; ₹3,000 respectively.
(B) ₹9,000; ₹2,700; ₹4,500 respectively.
(C) ₹4,800; ₹2,700; ₹2,100 respectively.
(D) ₹7,200; ₹2,700; ₹4,500 respectively. *(C.B.S.E. Sample Paper, 2021)*

Q. 108. A Company forfeited the following shares :
200 shares of ₹10 each; called up ₹9 per share, paid-up ₹7 per share. Journal Entry for forfeiture will be :

(A) Share Capital A/c	Dr.	2,000	
To Share Forfeiture A/c			200
To Calls in Arrears A/c			1,800
(B) Share Capital A/c	Dr.	2,000	
To Share Forfeiture A/c			1,800
To Calls in Arrears A/c			200
(C) Share Capital A/c	Dr.	1,800	
To Share Forfeiture A/c			1,400
To Calls in Arrears A/c			400
(D) Share Capital A/c	Dr.	1,800	
To Share Forfeiture A/c			400
To Calls in Arrears A/c			1,400

Q. 1[illegible] *X* Ltd. forfeited 500 shares of ₹10 each, ₹7 called up, issued at a premium of ₹2 per share to be paid at the time of allotment for non-payment of first call of ₹2 per share. Entry on forfeiture will be :

(A) Share Capital A/c	Dr.	3,500	
Securities Premium Reserve A/c	Dr.	1,000	
To Share First Call A/c			1,000
To Share Forfeiture A/c			3,500

(B) Share Capital A/c	Dr.	4,500	
Securities Premium Reserve A/c	Dr.	1,000	
To Share First Call A/c			1,000
To Share Forfeiture A/c			4,500

(C) Share Capital A/c	Dr.	4,500	
To Share First Call A/c			1,000
To Share Forfeiture A/c			3,500

(D) Share Capital A/c	Dr.	3,500	
To Share First Call A/c			1,000
To Share Forfeiture A/c			2,500

Q. 110. The amount of discount on reissue of forfeited shares cannot exceed :

(A) 5% of the face value
(B) 10% of the face value
(C) The amount received on forfeited shares
(D) The amount not received on forfeited shares

Q. 111. Discount allowed on re-issue of forfeited shares is debited to :

(A) Share Capital A/c (B) Share forfeiture A/c
(C) Statement of Profit & Loss (D) General Reserve A/c

Q. 112. The balance of the forfeited shares account after re-issue of forfeited shares is transferred to :

(A) Statement of Profit & Loss (B) Share Capital A/c
(C) Capital Reserve A/c (D) General Reserve A/c

Q. 113. *X* Ltd. forfeited 500 shares of ₹10 each fully called up for non-payment of final call of ₹3 per share 300 of these shares were reissued at ₹9 per share, fully paid up. What is the amount to be transferred to Capital Reserve Account?

(A) ₹3,500 (B) ₹2,100
(C) ₹3,200 (D) ₹1,800

Q. 114. *Y* Ltd. forfeited 400 shares of ₹10 each, ₹7 called up, for non-payment of first call of ₹2 per share. Out of these, 300 shares were reissued for ₹6 per share as ₹7 paid up. What is the amount to be transferred to Capital Reserve Account?

(A) ₹1,700 (B) ₹1,200
(C) ₹2,100 (D) ₹ 300

Q. 115. 400 shares of ₹10, on which ₹8 has been called and ₹5 has been paid, are forfeited. Out of these, 300 shares are re-issued for ₹9 as fully paid. What is the amount to be transferred to Capital Reserve Account?

(A) ₹1,200 (B) ₹1,600
(C) ₹2,000 (D) ₹1,700

Q. 116. *R* Ltd. forfeited 600 shares of ₹100 each ₹70 called up on which Mahesh has paid application and allotment money of ₹50 per share. Of these, 400 shares were re-issued to Naresh as fully paid-up for ₹110 per share. What is the amount to be transferred to Capital Reserve?

(A) ₹30,000 (B) ₹36,000
(C) ₹24,000 (D) ₹20,000

Q. 117. Madhu Ltd. forfeited 800 shares of ₹10 each issued at 10% premium to Shyam (₹9 called up) on which he did not pay ₹3 of allotment (including premium) and first call of ₹2. Out of these, 600 shares were re-issued to Ram as fully paid up for ₹9 per share. What is the amount to be transferred to capital Reserve?

(A) ₹2,400 (B) ₹1,800
(C) ₹3,000 (D) ₹3,600

Q. 118. Ronaldo Ltd. forfeited 300 equity shares of ₹10 each, fully called up, on which ₹5 per share (including premium of ₹1 per share) was received. It later reissued these shares at a discount.

The maximum discount per share, which the company could have given on their reissue would be:

(A) ₹6 per share (B) ₹5 per share
(C) ₹4 per share (D) ₹3 per share

(I.S.C. Sample Paper, 2021)

Q. 119. A Company forfeited 1,000 shares of ₹10 each fully called, on which ₹6,000 has been paid. Out of these 800 shares were reissued upon payment of ₹6,600. What is the amount to be transferred to Capital Reserve?

(A) ₹4,800 (B) ₹6,000
(C) ₹4,600 (D) ₹3,400

Q. 120. A company forfeited 700 shares of ₹10 each, on which only ₹5 per share was paid. Of these, 200 shares were reissued at ₹9 per share. Amount from Share Forfeiture Account to Capital Reserve Account will be transferred :

(A) ₹ 800 (B) ₹ 200
(C) ₹3,500 (D) ₹2,500

Q. 121. 300 equity shares of ₹10 each were issued at ₹5 per share premium. Only ₹4 per share on application has been paid on these shares. These shares were forfeited. Later on out of these, 200 shares were reissued at ₹12 per share as fully paid. What will be amount of Capital Reserve?

(A) ₹ 500 (B) ₹1,200
(C) ₹ 200 (D) ₹ 800

Q. 122. 700 shares of ₹10 each were reissued as ₹9 paid up for ₹7 per share. Entry for reissue will be :

(A) Bank A/c	Dr.	4,900	
Share Discount A/c	Dr.	1,400	
To Share Capital A/c			6,300

(B) Bank A/c	Dr.	4,900	
To Share Capital A/c			4,900
(C) Bank A/c	Dr.	4,900	
Share Forfeiture A/c	Dr.	1,400	
To Share Capital A/c			6,300
(D) Bank A/c	Dr.	4,900	
Share Forfeiture A/c	Dr.	2,100	
To Share Capital A/c			7,000

Q. 123. *A* Ltd. forfeited 2,000 shares of ₹10 each fully called up for non-payment of final call of ₹2 per share. 1,200 of these shares were reissued at ₹7 per share, fully paid up. What is the amount to be transferred to Capital Reserve Account?

(A) ₹ 7,600 (B) ₹ 1,200
(C) ₹12,400 (D) ₹ 6,000

Q. 124. Using information given in Q. 123 what is the net balance in Share Forfeiture Account :

(A) ₹ 9,600 (B) ₹6,400
(C) ₹16,000 (D) ₹2,800

HOTS

Q. 125. *B* Ltd. forfeited 300 shares of ₹100 each, ₹70 called up, for non-payment of first call of ₹20 per share. Out of these, 200 shares were reissued for ₹60 per share as ₹70 paid up. What is the amount to be transferred to Capital Reserve Account?

(A) ₹13,000 (B) ₹ 8,000
(C) ₹ 2,000 (D) ₹ 7,000

Q. 126. 2,000 shares of ₹10, on which ₹7 has been called and ₹5 has been paid, are forfeited. Out of these, 1,500 shares are re-issued for ₹9 as fully paid. What is the amount to be transferred to Capital Reserve Account?

(A) ₹ 6,000 (B) ₹7,500
(C) ₹10,000 (D) ₹8,500

Q. 127. *X* Ltd. forfeited 400 shares of ₹20 each ₹15 called up on which application and allotment money of ₹11 per share has been received. Of these, 100 shares were re-issued as fully paid-up for ₹24 per share. What is the amount to be transferred to Capital Reserve?

(A) ₹1,500 (B) ₹4,400
(C) ₹1,100 (D) ₹3,500

Q. 128. Vishnu Ltd. forfeited 20 shares of ₹10 each, ₹8 called up, on which John had paid application and allotment money of ₹5 per share, of these, 15 shares were reissued to Parker as fully paid up for ₹6 per share. What is the balance in the share Forfeiture Account after the relevant amount has been transferred to Capital Reserve Account?

(A) ₹ 0
(B) ₹ 5
(C) ₹25
(D) ₹100

(C.B.S.E. Sample Paper, 2021)

HOTS

Q. 129. *Z* Ltd. forfeited 300 shares of ₹10 each issued at 20% premium (₹9 called up) on which ₹4 of allotment (including premium) and first call of ₹2 has not been received. Out of these, 100 shares were re-issued as fully paid up for ₹9 per share. What is to amount to be transferred to capital Reserve?

(A) ₹400
(B) ₹300
(C) ₹500
(D) ₹600

Q. 130. Using information given in Q. 129, what is the net balance left in Share Forfeiture Account :

(A) ₹1,400
(B) ₹1,500
(C) ₹ 900
(D) ₹1,000

Q. 131. *P* Ltd. forfeited 150 shares of ₹10 each, issued at a premium of ₹2, for non-payment of the final call of ₹3. Out of these, 100 shares were re-issued at ₹11 per share. How much amount would be transferred to capital reserve?

(A) ₹ 700
(B) ₹500
(C) ₹1,200
(D) ₹300

HOTS

Q. 132. *XY* Limited issued 2,50,000 equity shares of ₹10 each at a premium of ₹1 each payable as ₹2.5 on application, ₹4 on allotment and balance on the first and final call. Applications were received for 5,00,000 equity shares but the company allotted to them only 2,50,000 shares. Excess money was applied towards amount due on allotment. Last call on 500 shares was not received and shares were forfeited after due notice. This is a case of :

(A) Over subscription
(B) Pro-rata allotment
(C) Forfeiture of Shares
(D) All of the above

Q. 133. Metacaf Ltd. issued 50,000 shares of ₹100 each payable ₹20 on application (on 1st May 2012); ₹30 on allotment (on 1st January 2013); ₹20 on first call (on 1st July 2013) and the balance on final call (on 1st February 2014). Shankar, a shareholder holding 5,000 shares did not pay the first call on the due date. The second call was made and Shankar paid the first call amount along with the second call. All sums due were received.

Total amount received on 1st February was :

(A) ₹15,00,000
(B) ₹16,00,000
(C) ₹10,00,000
(D) ₹11,00,000

(C.B.S.E. Sample Paper, 2015)

Q. 134. Harish Ltd. forfeited 500 shares of ₹100 each issued at 40% premium (₹70 called up) on which application & allotment of ₹80 each (including premium) has been received. Out of these, 200 shares were reissued for ₹65 per share (₹70 paid up). What is the amount to be transferred to Capital Reserve?

(A) ₹15,000
(B) ₹4,500
(C) ₹ 2,000
(D) ₹7,000

Q. 135. A Company forfeited 1,000 shares of ₹10 each fully paid on which ₹7,000 has been paid. Out of these 800 shares were reissued upon payment of ₹7,600. Amount transferred to Capital Reserve will be :

(A) ₹6,600 (B) ₹9,000

(C) ₹5,200 (D) ₹7,600

Q. 136. 1,000 shares of ₹10 each issued at 30% premium (to be paid on allotment) were forfeited for non-payment of ₹2 per share on first call and ₹2 per share on final call. Share Forfeiture Account will be credited with :

(A) ₹3,000 (B) ₹6,000

(C) ₹4,000 (D) ₹9,000

Q. 137. Raja Ltd. forfeited 300 shares of ₹100 each, ₹75 called up, for non-payment of first call of ₹20 per share. All these shares were reissued for ₹....... per share as ₹75 paid up. If amount transferred to Capital Reserve is ₹40 per share then what is the reissue price?

(A) ₹55 per share (B) ₹45 per share

(C) ₹60 per share (D) ₹40 per share

Q. 138. Pragya Ltd. forfeited 8,000 equity shares of ₹100 each issued at a premium of 10% for non-payment of first and final call of ₹30 per share. The maximum amount of discount at which these shares can be reissued will be :

(A) ₹ 80,000 (B) ₹3,20,000

(C) ₹5,60,000 (D) ₹2,40,000

(C.B.S.E. 2020, Kolkata, Lucknow)

Q. 139. The directors of Axim Ltd. forfeited 20,000 equity shares of ₹10 each, ₹8 per share called up for non-payment of first call of ₹2 per share. Final call of ₹2 per share has not been yet called. Half of the forfeited shares were reissued as fully paid up for ₹15 per share. The amount transferred to Capital Reserve will be :

(A) ₹2,00,000 (B) ₹1,20,000

(C) ₹ 60,000 (D) ₹ 40,000

(C.B.S.E. 2020, Kolkata, Lucknow)

Q. 140. On forfeiture of 100 shares of ₹50 each, ₹2,500 were credited to share forfeited account. These shares were re-issued at ₹25 per share fully paid up. The amount credited to 'Capital Reserve Account' will be :

(A) ₹2,500 (B) ₹5,000

(C) No amount (D) ₹3,000

(C.B.S.E. 2020, Kerala)

Q. 141. ABC Ltd. forfeited 4,000 shares of ₹10 each, fully called up, on which only application money of ₹3 has been paid. Out of these 2,000 shares were reissued and ₹4,000 has been transferred to capital reserve. Calculate the rate at which these shares were reissued.

(A) ₹10 Per share (B) ₹4 Per share

(C) ₹ 9 Per share (D) ₹8 Per share

(ISC Sample Paper, 2021)

Q. 142. What will be the correct sequence of events?

(*i*) Forfeiture of shares.
(*ii*) Default on Calls.
(*iii*) Re-issue of shares.
(*iv*) Amount transferred to capital reserve.

Options :

(A) (*i*), (*iv*), (*ii*), (*iii*)
(B) (*ii*), (*iv*), (*i*), (*iii*)
(C) (*ii*), (*i*), (*iii*), (*iv*)
(D) (*iii*), (*iv*), (*i*), (*ii*)

(C.B.S.E. Sample Paper, 2021)

Q. 143. The Interest on Calls-in-arrears Account is closed by:

(A) Crediting it to Statement of Profit & Loss
(B) Crediting it to Profit & Loss Appropriation Account
(C) Debiting it to Profit & Loss Appropriation Account
(D) Debiting it to Statement of Profit & Loss *(ISC Sample Paper, 2021)*

(See Answers at the end of the book.)

7

Company Accounts — Issue of Debentures

LEARNING OBJECTIVES

After studying this Chapter you should be able to understand :

- **Meaning and Features of a Debenture**
- **Types of Debentures**
- **Distinction between a Share and a Debenture**
- **Issue of Debentures for Cash at Par, at a Premium and at a Discount**
- **Issue of Debentures for Consideration Other than Cash**
- **Issue of Debentures as Collateral Security**
- **Accounting for Issue of Debentures Considering the Terms and Conditions of Redemption**
- **Writing off Loss/Discount on Issue of Debentures.**

Meaning of Debenture :

In addition to raising of Capital by issue of shares, a Company requiring funds on long term basis, may borrow money by issue of debentures. A debenture issued by a Company is usually in the form of a Certificate, given under the seal of the Company. Thus a debenture is a written acknowledgement of a debt taken by the Company as these are issued under the seal of the Company.

A Debenture Certificate contains the terms of the repayment of the principal sum at a specified date and the terms of payment of interest at a fixed per cent.

According to section 2(30) of the Companies Act, 2013 ''Debenture includes debenture stock, bonds and any other securities of a Company, whether constituting a charge on the assets of the Company or not.''

Characteristics or features of debentures :

1. A debenture is issued by a Company in the form of a Certificate, which is a written acknowledgement of debt taken by the Company.

2. A debenture is issued under the seal of the company.

3. It contains a contract for the repayment of principal sum at a specified date.

4. As per Companies Act, 2013 no Company is allowed to issue debentures having a maturity date of more than 10 years from the date of issue. However, a Company engaged in infrastructure projects can issue debentures for more than 10 years but not exceeding 30 years.

5. Usually the debentures are issued with a specified rate of interest, which is called 'Coupon Rate'. A debentureholder receives interest on his debentures at this specified rate, as mentioned in the certificate. Payment of interest is made, normally after every six months, whether the Company makes a profit or not.

6. A debenture is generally secured by a charge on the assets of the Company. This means that if the Company is unable to repay the debentures as per the terms of issue, the debentureholders can move the Court and realise their money by getting the assets of Company sold.

7. Funds raised by the issue of debentures are of long term nature and usually the debentures are repaid after a long period, such as seven years, ten years or twelve years. As such, the loan raised by the issue of debentures is also called as 'Loan Capital'.

Bond : It is very much similar to that of debenture. Traditionally, bonds had been issued by the government, but now a days these are also being issued by various semi-government and non-government organisations. Main distinction between debenture and bond is with respect to the rate of interest. Debentures are issued with a fixed rate of interest whereas bonds can be issued without predetermined rate of interest as in the case of **deep discount bonds or zero coupon bonds.** A deep discount bond or zero coupon bond is one which is issued without prefixed rate of interest and its issue price is heavily discounted. The difference between issue price and the redemption price represents the total interest to be spread over the duration of the bond. A proportionate amount of total interest is charged to Statement of Profit and Loss every year over the lifetime of bond.

Types or Kinds of Debentures :

A Company may issue the following types of debentures :

1. **Secured or Mortgage Debentures** : These debentures are those which are secured either on particular assets of the Company called fixed charge or on all assets of the Company in general, called a floating charge. Fixed charge denies the Company from dealing with mortgaged assets, whereas the floating charge does not prevent the Company from using the assets. If the Company is unable to repay the debentures on the due date, the debentureholders can realise their money from the assets mortgaged with them. First mortgage debentures are those that have a first claim on the assets charged and second mortgage debentures are those having a second claim on the assets charged. In India, debentures have necessarily to be secured.

2. **Unsecured or Naked Debentures** : These debentures are those which are not given any security. The holders of such debentures are treated as unsecured creditors at the time of liquidation of the Company. Such debentures are not very common these days, so much so that, unless otherwise stated, a debenture is presumed to be secured.

3. **Registered Debentures** : Names and addresses of the holders of such debentures are recorded in a register of the Company called, "Register of Debentureholders". Such debentures are not freely transferable. The Transfer of such debentures requires the execution of a proper transfer deed. Principal amount and interest on such a debenture is paid to the person whose name appears in the Company's register.

4. **Bearer Debentures** : Names and addresses of the holders of such debentures are not recorded in the Company and these debentures are transferable by mere

delivery. Payment of principal and interest is made to the bearer of such debentures. Coupons are attached with these debentures and the interest is paid to such persons who produce the coupons in the specified bank.

5. **Redeemable Debentures** : Redeemable debentures are those debentures which will be repaid by the Company either in lump sum at the end of a specified period or by instalments during the lifetime of the Company. Most of the debentures are generally of this type.

6. **Irredeemable or Perpetual Debentures** : Irredeemable debentures are those debentures which are not repayable by the Company during its life time. These debentures are repayable only at the time of liquidation of the Company.

7. **Convertible Debentures** : Convertible debentures are those debentures which are convertible into equity shares or other securities at a stated rate of exchange either at the option of debentureholders or at the option of the company after a specified period. When only a part of the amount of debenture is convertible into shares, such debentures are called 'Partly Convertible Debentures'. When the full amount of debenture is convertible into shares, such debentures are called 'Fully Convertible Debentures'. SEBI Guidelines require that where the conversion is to be made at or after 18 months from the date of allotment but before 36 months, any conversion in part or whole shall be optional on the part of the debentureholders. Convertible debentures are very popular these days, as they provide liquidity, safety, capital appreciation and assured return to the investors.

Distinction Between a Share and a Debenture

Basis of Distinction	*Share*	*Debenture*
1. **Capital *vs* Loan**	A share is a part of the Capital of the Company, therefore, the shareholders are the owners of the Company.	A debenture is a part of the loan and as such, the debentureholders are the creditors of the Company.
2. **Dividend *vs* Interest**	A shareholder gets dividend from the Company.	A debentureholder gets interest from the Company.
3. **Fluctuating or Fixed rate of dividend or interest**	Dividend is paid only when there are profits. The rate of dividend may fluctuate from year to year depending upon the profits and decision of the directors.	The rate of interest is fixed and it must be paid irrespective of the Company making a profit or incurring a loss.
4. **Voluntary or compulsory redemption**	It is at the option of the Company to return the amount of shares by buying back its own shares.	The amount of debentures must be returned according to the terms of the issue.
5. **Priority of repayment of principal in case of winding up**	In the case of winding up, the payment of share capital is made **after the repayment of debentures.**	In the case of winding up, the payment of debentures is made **before the payment of share capital.**
6. **Unsecured or Secured**	A share is always unsecured. Hence, they bear more risk.	Debentures are usually secured on the assets of the Company. Hence, they bear little risk.

7.	**Restriction on issue at discount**	Under Section 53 of the Companies Act 2013, shares cannot be issued at discount except sweat equity shares.	There are no restrictions on the issue of debentures at discount.
8.	**Voting rights**	Share confers on its holder the right to participate in and vote at Company's meetings.	A holder of debenture neither possesses any voting right in the Company's meetings nor can he participate in the meeting.

Issue of Debentures

The procedure for the issue of debentures is very much similar to that of the issue of shares. A prospectus is issued in which terms and conditions of the issue of debentures are given. Applications on the prescribed form are deposited with the Company's bankers along with application money. Full amount of debentures may be called by the Company on application itself or the amount may be called in instalments, as in the case of shares. If the amount of debenture is called in instalments, some amount may be called on application, some amount on allotment and the balance may be called in one or more calls.

As per Section 39 of the Companies Act, 2013, Condition of minimum subscription applies on every type of securities including debentures.

Debentures may be issued either at par, or at a premium or at a discount. There are no restrictions on the issue of debentures at discount, whereas shares cannot be issued at discount. The rate of discount is also to be decided by the directors.

Journal entries on issue of debentures are also the same as in the case of issue of shares. The only difference is that 'Debenture A/c' will be opened in place of 'Share Capital A/c'. It is usual to prefix the rate of interest to the debentures. Thus, if the rate of interest is 12%, the name given will be "12% Debentures".

Following entries will be passed on the issue of debentures (assuming that the debentures carry 12% interest)

1. On receipt of application money :
   Bank A/c Dr.
   To 12% Debenture Application A/c
   (Application money received)

2. On Transfer of application money to Debenture Account :
   12% Debenture Application A/c Dr.
   To 12% Debentures A/c
   (Application money transferred)

3. On refund of money on totally rejected applications :
   12% Debenture Application A/c Dr.
   To Bank A/c
   (Application money returned on rejected applications)

4. On the transfer of surplus application money on partially accepted applications :
   12% Debenture Application A/c Dr.
   To 12% Debenture Allotment A/c
   (Transfer of excess application money to allotment A/c)

5. On making allotment money due :
12% Debenture Allotment A/c Dr.
To 12% Debentures A/c
(Allotment money due)

6. On receipt of allotment money :
Bank A/c Dr.
To 12% Debenture Allotment A/c
(Allotment money received)

7. On making the call money due :
12% Debenture First Call A/c Dr.
To 12% Debentures A/c
(First Call money due)

8. On receipt of call money :
Bank A/c Dr.
To 12% Debenture First Call A/c
(First Call money received)

If there are more than one call, separate entries for each call will be passed, like above.

Issue of Debentures at Par

ILLUSTRATION 1.

Govind Ltd. issued 5,000, 12% Debentures of ₹100 each, at par, payable as follows :

On Application ₹20; On Allotment ₹20; On First Call ₹30; and On Final Call ₹30.

Public applied for 6,000 debentures. Applications for 4,500 debentures were accepted in full. Applications for 800 debentures were allotted 500 debentures and applications for 700 debentures were rejected. Money overpaid on applications was utilised towards allotment.

Pass journal entries assuming that all moneys due were duly received, except final call on 200 debentures.

SOLUTION : JOURNAL OF GOVIND LTD.

Date	*Particulars*		*L.F.*	*Dr.*	*Cr.*
				₹	₹
	Bank A/c	Dr.		1,20,000	
	To 12% Debenture Application A/c				1,20,000
	(Application money received on 6,000 debentures @ ₹20 each)				
	12% Debenture Application A/c	Dr.		1,20,000	
	To 12% Debentures A/c				1,00,000
	To 12% Debenture Allotment A/c				6,000
	To Bank A/c				14,000
	(Application money transferred)				

12% Debenture Allotment A/c To 12% Debentures A/c (Allotment money due on 5,000 debentures @ ₹20 each)	Dr.	1,00,000	1,00,000
Bank A/c To 12% Debenture Allotment A/c (Balance of allotment money received, *i.e.*, ₹1,00,000 – ₹6,000)	Dr.	94,000	94,000
12% Debenture First Call A/c To 12% Debentures A/c (First Call due)	Dr.	1,50,000	1,50,000
Bank A/c To 12% Debenture First Call A/c (First Call money received)	Dr.	1,50,000	1,50,000
12% Debenture Second & Final Call A/c To 12% Debentures A/c (Second & Final Call due)	Dr.	1,50,000	1,50,000
Bank A/c Calls in Arrears A/c To 12% Debenture Second & Final Call A/c (Second & Final Call money received on 4,800 debentures @ ₹30 per Debenture)	Dr. Dr.	1,44,000 6,000	1,50,000

Issue of Debentures at Premium

When the debentures are issued at more than their face value, they are said to have been issued at premium. For example, if a debenture of ₹100 is issued at ₹110, ₹10 is the premium, which is a gain to the Company. This premium should not be treated as a revenue profit as it is not an income arising from the normal course of business operations. It is a capital profit and should, therefore, be used in writing off the capital losses, such as discount on issue of shares and debentures, premium on redemption of debentures, preliminary expenses, goodwill, patents etc.

As stated earlier, the name of 'Share Premium A/c' has been changed to 'Securities Premium A/c'. Since the Debentures are also securities, Debentures Premium should also be credited to 'Securities Premium Reserve A/c'.

"Securities Premium Reserve A/c" is shown on the equity & liabilities side of the balance sheet under the head "Reserves and Surplus".

ILLUSTRATION 2.

Traditional Products Ltd. offered 20,000, 8% Debentures of ₹500 each at a premium of 10% payable as ₹200 on application (including premium) and balance on allotment, redeemable at par after 8 years. But applications are received for 30,000 debentures and the allotment is made on pro-rata basis. All the money due on application and allotment is received. Record necessary entries regarding issue of debentures.

SOLUTION: JOURNAL OF TRADITIONAL PRODUCTS LTD.

Date	Particulars		L.F.	Dr	Cr
				₹	₹
	Bank A/c	Dr.		60,00,000	
	To 8% Debenture Application A/c				60,00,000
	(Application money received on 30,000 debentures @ ₹200 each)				
	8% Debenture Application A/c	Dr.		60,00,000	
	To 8% Debentures A/c				30,00,000
	To Securities Premium Reserve A/c				10,00,000
	To 8% Debenture Allotment A/c				20,00,000
	(Transfer of application money)				
	8% Debenture Allotment A/c	Dr.		70,00,000	
	To 8% Debentures A/c				70,00,000
	(Allotment due on 20,000 debentures @ ₹350 each)				
	Bank A/c	Dr.		50,00,000	
	To 8% Debenture Allotment A/c				50,00,000
	(Allotment money received)				

Issue of Debentures at Discount

When the Company issues debentures at a price which is less than their face or nominal value, the debentures are said to have been issued at a discount. There are no restrictions in the Companies Act regarding the maximum limit for discount on debentures.

Treatment of Discount/Loss on Issue of Debentures

As per AS-16, borrowing costs and discount on issue or premium on redemption relating to borrowing could be amortized over loan period.

Unamortized portion of such expenses be shown on the assets side of the balance sheet under the head 'Current/Non Current Assets' depending on whether the amount will be amortized in the next 12 months or thereafter.

For example, if the Discount or Loss on Issue of Debentures amounts to ₹1,20,000 and it is to be written off in six years, then :

₹20,000 shall be debited to Statement of Profit & Loss of the Current year;

₹20,000 shall be shown under 'Other Current Assets', and the balance ₹80,000 shall be shown under 'Other Non Current Assets'.

Discount or Loss on Issue of Debentures is a capital loss. It should be written off as early as possible but within the lifetime of the debentures. It can be written off by debiting first to Securities Premium Reserve Account or from Capital Reserve or from Statement of Profit or Loss in that order. Following entry is passed for writing off discount or loss on issue of debentures :

Securities Premium Reserve A/c Dr.
Or
Capital Reserve A/c Dr.
Or
Statement of Profit & Loss Dr.
To Discount/Loss on Issue of Debentures A/c

Discount being a loss, is recorded in the books of the Company by debiting "Discount on Issue of Debentures A/c". Discount is generally recorded at the time of allotment entry.

ILLUSTRATION 3.

Surya Ltd. issued 2,500, 15% Debentures of ₹100 each at a discount of 10% payable as follows:

₹25 on application; ₹25 on allotment and the balance on First Call.

Applications were received for 2,000 debentures and the allotment was made. All the moneys were duly received. Directors decided to write off 1/5th of "Discount on Issue of Debentures A/c" from Statement of Profit and Loss each year.

Pass journal entries (for first year only) and present the relevant information in the Balance Sheet at the end of the first year.

SOLUTION : JOURNAL OF SURYA LTD.

Date	*Particulars*		*L.F.*	*Dr.*	*Cr*
				₹	₹
	Bank A/c	Dr.		50,000	
	To 15% Debenture Application A/c				50,000
	(Application money received for 2,000 debentures @ ₹25 each)				
	15% Debenture Application A/c	Dr.		50,000	
	To 15% Debentures A/c				50,000
	(Application money transferred)				
	15% Debenture Allotment A/c	Dr.		50,000	
	Discount on Issue of Debentures A/c	Dr.		20,000	
	To 15% Debentures A/c				70,000
	(Allotment due)				
	Bank A/c	Dr.		50,000	
	To 15% Debentures Allotment A/c				50,000
	(Amount received on allotment)				
	15% Debentures First & Final Call A/c	Dr.		80,000	
	To 15% Debentures A/c				80,000
	(First & Final Call due)				
	Bank A/c	Dr.		80,000	
	To 15% Debentures First & Final Call A/c				80,000
	(Amount received on First & Final Call)				
	Statement of Profit & Loss	Dr.		4,000	
	To Discount on Issue of Debentures A/c				4,000
	(1/5th of Discount on debentures written off)				

An Extract of BALANCE SHEET OF SURYA LTD.
at the end of first year

Particulars	*Note No.*	*Current Year*	*Previous Year*
I. EQUITY AND LIABILITIES		₹	₹
Shareholder's Funds :			
(*a*) Share Capital			
(*b*) Reserve and Surplus	1	(4,000)	
Non Current Liabilities :			
Long term Borrowings	2	2,00,000	
II. ASSETS			
(*a*) **Non Current Assets :**			
Other Non Current Assets	3	12,000	
(*b*) **Current Assets :**			
Other Current Assets	4	4,000	

Notes to Accounts :

		₹
(1) **Reserve and Surplus :**		
Balance in Statement of Profit & Loss		—
Less : Discount on Issue of Debentures written off		(4,000)
(2) **Long term Borrowings :**		
15% Debentures		2,00,000
(3) **Other Non Current Assets :**		
Discount on Issue of Debentures	20,000	
Less : Written off from Statement of Profit & Loss	4,000	
	16,000	
Less : To be written off next year	4,000	12,000
(4) **Other Current Assets :**		
Discount on Issue of Debentures (to be written off next year)		4,000

It should be noted that in case, the full amount of a debenture is received in one instalment, the amount should be credited to 'Debenture Application & Allotment A/c', instead of 'Debenture Application A/c'.

Issue of Debentures for Consideration other than Cash

Just like shares debentures may also be issued for consideration other than Cash, in the following circumstances :

(1) Issue of Debentures to Promoters :

Promoters of a Company may be issued debentures in the Company for the services rendered by them. The entry will be :

Incorporation Costs or Formation Exp. A/c Dr.
To Debentures A/c
(Debentures issued to Promoters)

(2) Issue of Debentures to Underwriters :

The Company may allot debentures to the underwriters to pay their commission. The entries will be :

(*i*) Underwriting Commission A/c Dr.
To Underwriters A/c
(Underwriting Commission due)

(*ii*) Underwriters A/c Dr.
To Debentures A/c
(Allotment of debentures to Underwriters for the Commission due to them)

(3) Issue of Debentures to Vendors :

Sometimes a Company purchases some assets from the vendor and instead of paying the vendor in cash, the Company may decide to issue debentures to the vendor in payment of purchase consideration. Such an issue of debentures to vendors is known as issue of debentures for consideration other than cash. Debentures can be issued to vendors at par, at a premium or at a discount. Following entries will be passed for this purpose :

1. On purchase of assets :

Assets A/c Dr.
To Vendor's A/c

2. I. For the issue of debentures to vendor at par :

Vendor's A/c Dr.
To Debentures A/c

II. For the issue of debentures to vendor at premium :

Vendor's A/c Dr.
To Debentures A/c
To Securities Premium Reserve A/c

III. For the issue of debentures to vendor at discount :

Vendor's A/c Dr.
Discount on Issue of Debentures A/c Dr.
To Debentures A/c

ILLUSTRATION 4.

A company purchased assets of the book value of ₹99,000 from another Co. It was agreed that the purchase consideration be paid by issuing 11% Debentures of ₹100 each. Assume that the debentures have been issued (*i*) at par, (*ii*) at a discount of 10%, and (*iii*) at a premium of 10%.

Give necessary journal entries in the books of purchasing company assuming that the discount on issue is to be written off in the first year.

SOLUTION : JOURNAL

Date	Particulars		L.F.	Dr.	Cr.
				₹	₹
	Sundry Assets A/c	Dr.		99,000	
	To Vendors' A/c				99,000
	(Assets purchased)				
(1)	When Debentures are issued at par :				
	Vendors' A/c	Dr.		99,000	
	To 11% Debentures A/c				99,000
	(Issue of debentures at par)				
(2)	When Debentures are issued at Discount :				
	Vendors' A/c	Dr.		99,000	
	Discount on Issue of Debentures A/c	Dr.		11,000	
	To 11% Debentures A/c				1,10,000
	(Issue of 1,100 debentures of ₹100 each at 10% discount calculated as follows : $\frac{99,000}{90}$ = 1,100 debentures)				
	Statement of Profit & Loss	Dr.		11,000	
	To Discount on Issue of Debentures A/c				11,000
	(Discount on issue of debentures written off)				
(3)	When debentures are issued at premium :				
	Vendors' A/c	Dr.		99,000	
	To 11% Debentures A/c				90,000
	To Securities Premium Reserve A/c				9,000
	(Issue of 900 debentures of ₹100 each at 10% premium, calculated as follows : $\frac{99,000}{110}$ = 900 debentures)				

ILLUSTRATION 5.

Mona Ltd. acquired assets of ₹50 lakhs and took over creditors of ₹5 lakhs from Ram Enterprises. Mona Ltd. issued 8% Debentures of ₹100 each at a premium of 25% as purchase consideration. Record necessary journal entries in the books of Mona Ltd.

SOLUTION : JOURNAL OF MONA LTD.

Date	Particulars		L.F.	Dr.	Cr.
				₹	₹
	Assets A/c	Dr.		50,00,000	
	To Creditors				5,00,000
	To Ram Enterprises				45,00,000
	(Purchase of assets and creditors from Ram Enterprises)				
	Ram Enterprises	Dr.		45,00,000	
	To 8% Debentures A/c				36,00,000
	To Securities Premium Reserve A/c				9,00,000
	(Issue of 36,000 Debentures of ₹100 each at 25% premium, calculated as $\frac{45,00,000}{125}$ = 36,000)				

ILLUSTRATION 6.

Zee Ltd. purchased a running business from Rainbow Ltd. for a sum of ₹6,60,000. Zee Ltd. paid 5% of the purchase consideration by drawing a Promissory Note in favour of Rainbow Ltd. and the balance by the issue of fully paid 7% Debentures of ₹100 each at a premium of 10%. The assets and liabilities of Rainbow Ltd. consisted of :

	₹
Fixed Assets	6,50,000
Sundry Creditors	80,000

You are required to pass the necessary journal entries in the books of Zee Ltd.

(I.S.C. 2020)

SOLUTION : JOURNAL OF ZEE LTD.

Date	*Particulars*		*L.F.*	*Dr. Amount*	*Cr. Amount*
				₹	₹
	Fixed Assets A/c	Dr.		6,50,000	
	Goodwill A/c (Balancing figure)	Dr.		90,000	
	To Sundry Creditors A/c				80,000
	To Rainbow Ltd.				6,60,000
	(Business purchased)				
	Rainbow Ltd.	Dr.		6,60,000	
	To Bills Payable A/c				33,000
	To 7% Debentures A/c				5,70,000
	To Securities Premium Reserve A/c				57,000
	(Payment made by accepting a B/P and by issuing 5,700 debentures of ₹100 each at 10% premium)				

Working Note :

	₹
Purchase Consideration	6,60,000
Less : 5% paid by issue of B/P	33,000
	6,27,000

No. of Debentures issued : $\frac{6,27,000}{110} = 5,700$

ILLUSTRATION 7.

Venus Ltd. took over assets of ₹10,00,000 and liabilities of ₹1,80,000 of Cayns Ltd. for ₹7,60,000. Venus Ltd. issued 9% Debentures of ₹100 each at a discount of 5% in full satisfaction of the purchase consideration in favour of Cayns Ltd.

Pass necessary journal entries in the books of Venus Ltd. for the above transactions. Venus Ltd. writes off all capital losses in the first year itself.

(C.B.S.E. 2018, Comptt.)

SOLUTION :

Books of Venus Ltd.

JOURNAL

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
(i)	Sundry Assets A/c	Dr.		10,00,000	
	To Sundry Liabilities A/c				1,80,000
	To Cayns Ltd.				7,60,000
	To Capital Reserve A/c (Balancing figure)				60,000
	(Business purchased from Cayns Ltd.)				
(ii)	Cayns Ltd.	Dr.		7,60,000	
	Discount on issue of Debentures A/c	Dr.		40,000	
	To 9% Debentures A/c				8,00,000
	(₹8,000, 9% Debentures of ₹100 each issued at a discount of 5%)				
	Capital Reserve A/c	Dr.		40,000	
	To Discount on Issue of Debentures A/c				40,000
	(Discount on issue of debentures written off)				

Working Note : Number of Debentures Issued = 7,60,000 ÷ 95 = 8,000

ILLUSTRATION 8.

Chrome Ltd. took over assets of ₹6,00,000 and liabilities of ₹40,000 of Polymer Ltd. at an agreed value of ₹6,30,000. Chrome Ltd. issued 10% Debentures of ₹100 each at a discount of 10% to Polymer Ltd. in full satisfaction of the price. Chrome Ltd. writes off any capital losses incurred during a year, at end of that financial year.

You are required to pass the necessary journal entries to record the above transactions in the books of Chrome Ltd. *(I.S.C. 2017)*

SOLUTION :

JOURNAL OF CHROME LTD.

Date	Particulars		L.F.	Dr.	Cr.
				₹	₹
	Sundry Assets A/c	Dr.		6,00,000	
	Goodwill A/c (Balancing Figure)	Dr.		70,000	
	To Sundry Liabilities A/c				40,000
	To Polymer Ltd.				6,30,000
	(Business Purchased)				
	Polymer Ltd.	Dr.		6,30,000	
	Discount on Issue of Debentures A/c	Dr.		70,000	
	To 10% Debentures A/c				7,00,000
	(Issue of 7,000 Debentures of ₹100 each at 10% discount)				
	Statement of Profit & Loss	Dr.		70,000	
	To Discount on Issue of Debentures A/c				70,000
	(Discount on issue of Debentures written off)				

$$\text{Number of Debentures} = \frac{6{,}30{,}000}{90} = 7{,}000$$

ILLUSTRATION 9.

D Ltd. purchased machinery for ₹2,00,000 from *E* Ltd. on 1st April 2019. 25% was paid by accepting a draft payable after three months and the balance was paid by issue of ₹1,60,000, 12% debentures in *D* Ltd. Pass the necessary journal entries for recording the transactions in the books of *D* Ltd.

SOLUTION :

JOURNAL OF *D* LTD.

Date	*Particulars*		*L.F.*	*Dr.* (₹)	*Cr.* (₹)
2019					
April 1	Machinery A/c	Dr.		2,00,000	
	To *E* Ltd.				2,00,000
	(Machinery purchased from *E* Ltd.)				
April 1	*E* Ltd.	Dr.		50,000	
	To Bills Payable A/c				50,000
	(Part payment made by accepting a bill of exchange)				
April 1	*E* Ltd.	Dr.		1,50,000	
	Discount on issue of Debentures A/c	Dr.		10,000	
	To 12% Debentures A/c				1,60,000
	(Balance amount of ₹1,50,000 settled by the issue of ₹1,60,000 debentures)				
2020					
March 31	Statement of Profit & Loss	Dr.		10,000	
	To Discount on Issue of Debentures A/c				10,000
	(Discount on issue of debentures written off)				

ILLUSTRATION 10.

Radha Ltd. purchased machinery for ₹4,00,000 from Krishna Ltd. on 1st April, 2022. ₹1,00,000 were paid immediately and the balance was paid by issue of ₹2,80,000 12% debentures in Radha Ltd. Pass the necessary journal entries for recording the transactions in the books of Radha Ltd.

SOLUTION :

JOURNAL OF RADHA LTD.

Date	*Particulars*		*L.F.*	*Dr.*	*Cr.*
2022				₹	₹
April 1	Machinery A/c	Dr.		4,00,000	
	To Krishna Ltd.				4,00,000
	(Machinery purchased from Krishna Ltd.)				
April 1	Krishna Ltd.	Dr.		1,00,000	
	To Bank A/c				1,00,000
	(Part payment made in Cash)				
April 1	Krishna Ltd.	Dr.		3,00,000	
	To 12% Debentures A/c				2,80,000
	To Securities Premium Reserve A/c				20,000
	(Balance amount of ₹3,00,000 settled by the issue of ₹2,80,000 debentures)				

ILLUSTRATION 11.

X Ltd. purchased assets of *Y* Ltd. as under :

Plant and Machinery of ₹20,00,000 at ₹18,00,000; Land and Buildings of ₹30,00,000 at ₹42,00,000 for purchase consideration of ₹55,00,000 and paid ₹10,00,000 in cash and remaining by issue of 8% Debentures of ₹100 each at a premium of 20%. Record necessary entries in the books of *X* Ltd.

SOLUTION :

Books of X Ltd.

JOURNAL

Date	*Particulars*		*L.F.*	*Dr.*	*Cr.*
				₹	₹
	Plant and Machinery A/c	Dr.		18,00,000	
	Land and Buildings A/c	Dr.		42,00,000	
	To Capital Reserve A/c (Balancing Figure)				5,00,000
	To *Y* Ltd.				55,00,000
	(Purchase of assets of *Y* Ltd.)				
	Y Ltd.	Dr.		10,00,000	
	To Bank A/c				10,00,000
	(Part payment made in cash)				
	Y Ltd.	Dr.		45,00,000	
	To 8% Debentures A/c				37,50,000
	To Securities Premium Reserve A/c				7,50,000
	(Issue of 37,500 Debentures of ₹100 each at 20% premium calculated as $\frac{45,00,000}{120} = 37,500$)				

ILLUSTRATION 12.

Neeraj Ltd. took over business of Ajay enterprises on 1-04-2020. The details of the agreement regarding the assets and liabilities to be taken over are :

Particulars	*Book Value (₹)*	*Agreed Value (₹)*
Building	20,00,000	35,00,000
Plant and Machinery	12,00,000	8,00,000
Stock	4,00,000	4,00,000
Trade receivables	5,00,000	4,00,000
Creditors	2,00,000	3,00,000
Outstanding Expenses	50,000	1,00,000

It was decided to pay for purchase consideration as ₹7,00,000 through Cheque and balance by issue of 2,00,000, 9% Debentures of ₹20 each at a premium of 25%. Journalize. *(C.B.S.E. Sample Paper, 2020)*

SOLUTION :

Journal of Neeraj Ltd.

Date	*Particulars*		*L.F.*	*Dr.* (₹)	*Cr.* (₹)
2020					
April 1	Building A/c	Dr.		35,00,000	
	Plant & Machinery A/c	Dr.		8,00,000	
	Stock A/c	Dr.		4,00,000	
	Trade Receivables A/c	Dr.		4,00,000	
	Goodwill A/c (Balancing Figure)	Dr.		10,00,000	
	To Creditors A/c				3,00,000
	To Outstanding Expenses A/c				1,00,000
	To Ajay Enterprises				57,00,000
	(Assets and liabilities of business taken over, recorded at agreed value)				
"	Ajay Enterprises	Dr.		57,00,000	
	To Bank A/c				7,00,000
	To 9% Debentures A/c				40,00,000
	To Securities Premium Reserve A/c				10,00,000
	(Purchase consideration paid to Ajay enterprises)				

Issue of Debentures as Collateral Security

Sometimes, when a Company takes a loan from a Bank or from some other party, the Company may have to issue debentures as a subsidiary or secondary security in addition to the principal security. In other words, collateral security means secondary security in addition to the principal security. The bank or the other persons to whom such debentures are issued as collateral security will not be entitled to any interest on these debentures. They are entitled to get interest on the original loan advanced by them. If a default is made either in the payment of interest or in the payment of principal debt, the lender will first realise its debt from the principal security. But if the full amount of debt is not realised from the principal security, it may claim all the rights of a debentureholder.

As soon as the Company pays the final instalment of loan, it can take its debentures back.

There are two methods of dealing with such debentures in the books of accounts of the Company :

(1) **First Method** : **When Company decided not to record the issue of Debentures as Collateral Security :** In this method, no entry need to be passed in the books of the Company, as the debentures are not actually issued, but only given away as collateral security. As such, under this method, entry is passed only for taking a loan. If the loan is taken from a bank, the entry will be :

Bank A/c Dr.
To Bank Loan A/c

On the equity & liabilities side of the balance sheet, a note is appended below the loan that the loan is secured by the issue of debentures as collateral security.

(2) **Second Method : When Company decided to record the issue of debentures as Collateral Security :** In this method, the entry for issuing debentures as Collateral Security is also recorded with the entry for taking the loan.

I. On taking a loan :

Bank A/c Dr.
To Bank Loan A/c

II. On issuing the debentures as collateral security :

Debentures Suspense A/c Dr.
To Debentures A/c

In the Balance Sheet, Debentures Suspense A/c will be shown as a deduction from the Debentures Account on the Equity & Liabilities side. As and when the loan is repaid, both the entries passed above are reversed.

ILLUSTRATION 13.

A Company had ₹10,00,000, 12% Debentures outstanding as on 1st April, 2021. During the year company took a loan of ₹2,00,000 from the State Bank of India for which the Company placed with the bank debentures for ₹2,50,000 as Collateral Security. Pass journal entries, if any. Also show how the Debentures and Bank Loan will appear in the Company's Balance Sheet on 31st March, 2022.

SOLUTION :

First Method : No entry is passed for the issue of debentures in this method. Entry is passed only for taking a loan from the bank, as under :

Bank A/c	Dr.	2,00,000	
To Bank Loan A/c			2,00,000
(Loan taken from the Bank and ₹2,50,000 debentures deposited as collateral security)			

EXTRACT OF BALANCE SHEET
as at 31st March, 2022

Particulars	*Note No.*	*Current Year*	*Previous Year*
I. EQUITY AND LIABILITIES		₹	₹
Non-Current Liabilities :			
Long-term Borrowings	1	12,00,000	10,00,000

Notes to Accounts :

	₹
(1) Long-term Borrowings :	
12% Debentures	10,00,000
(In addition, Debentures for ₹2,50,000 have been issued as collateral security)	
Bank Loan (On collateral security of Debentures of ₹2,50,000)	2,00,000
	12,00,000

Second Method : Following entries are passed in this method :

1.	Bank A/c	Dr.	2,00,000	
	To Bank Loan A/c			2,00,000
	(Loan taken from the Bank)			
2.	Debentures Suspense A/c	Dr.	2,50,000	
	To 12% Debentures A/c			2,50,000
	(Issue of ₹2,50,000 debentures as collateral security to secure a loan of ₹2,00,000 from the Bank)			

EXTRACT OF BALANCE SHEET *as at 31st March, 2022*

Particulars	*Note No.*	*Current Year*	*Previous Year*
I. EQUITY AND LIABILITIES		₹	₹
Non-Current Liabilities :			
Long-term Borrowings	1	12,00,000	10,00,000

Notes to Accounts :

		₹
(1) Long-term Borrowings :		
12% Debentures	12,50,000	
Less : Debentures Suspense A/c	2,50,000	10,00,000
Bank Loan (On collateral security of Debentures of ₹2,50,000)		2,00,000
		12,00,000

ILLUSTRATION 14.

Meghnath Limited took a loan of ₹1,20,000 from a bank and deposited 1,400, 8% debentures of ₹100 each as collateral security along with primary security worth ₹2 lakhs. Company again took a loan of ₹80,000 after two months from a bank and deposited 1,000, 8% debentures of ₹100 each as collateral security. Record necessary journal entries. How will you show the issue of Debentures and Bank Loan in the balance sheet of the company.

SOLUTION :

Books of Meghnath Ltd.

JOURNAL

Date	*Particulars*		*L.F.*	*Dr.*	*Cr.*
				₹	₹
When loan is taken	Bank A/c	Dr.		1,20,000	
	To Bank Loan A/c				1,20,000
	(Loan obtained from bank secured by primary security* worth ₹2,00,000 and ₹1,40,000, 8% debentures as collateral security)				
,,	Debenture Suspense A/c	Dr.		1,40,000	
	To 8% Debentures A/c				1,40,000
	(Issue of ₹1,40,000 debentures as collateral security to secure a loan of ₹1,20,000 from the bank)				

,,	Bank A/c Dr. To Bank Loan A/c (Loan obtained from bank secured by ₹1,00,000, 8% debentures as collateral security)		80,000	80,000
,,	Debenture Suspense A/c Dr. To 8% Debentures A/c (Issue of ₹1,00,000 debentures as collateral security to secure a loan of ₹80,000 from the bank)		1,00,000	1,00,000

Note : * No entry is passed for primary security in the books of accounts.

EXTRACT OF BALANCE SHEET OF MEGHNATH LTD.

as at ....

Particulars	*Note No.*	*Current Year*	*Previous Year*
I. EQUITY AND LIABILITIES		₹	₹
Non-Current Liabilities :			
Long-term Borrowings	1	2,00,000	

Notes to Accounts :

		₹
(1) **Long-term Borrowings :**		
8% Debentures	2,40,000	
Less : Debenture Suspense A/c	2,40,000	—
Bank Loan (On primary security worth ₹2,00,000 and collateral security of Debentures of ₹2,40,000)		2,00,000

ILLUSTRATION 15.

A Ltd. Company issued debentures of ₹1,00,000 which were issued as follows :

(1)	For cash at 90%	₹50,000 (Nominal)
(2)	For creditor for ₹20,000 Capital Expenditure in satisfaction of his claim	₹25,000 (Nominal)
(3)	To Bankers for a loan of ₹15,000 as collateral security	₹25,000 (Nominal)

Pass Journal Entries. (Ignore writing off discount on issue of debentures)

SOLUTION :

JOURNAL

Date	*Particulars*	*L.F.*	*Dr.*	*Cr.*
			₹	₹
(1) I.	Bank A/c Dr. To Debenture Application & Allotment A/c (Application money received)		45,000	45,000

II.	Debenture Application & Allotment A/c Dr. Discount on Issue of Debentures A/c Dr. To Debentures A/c (Transfer of application money to Debentures A/c, issued at 10% Discount)		45,000 5,000	 50,000
(2) I.	Fixed Assets A/c Dr. To Vendor's A/c (Capital Expenditure made for the purchase of Assets)		20,000	 20,000
II.	Vendor's A/c Dr. Discount on Issue of Debentures A/c Dr. To Debentures A/c (Debentures issued to vendors at discount)		20,000 5,000	 25,000
(3) I.	Bank A/c Dr. To Bank Loan A/c (Loan taken, secured by the issue of ₹25,000 debentures)		15,000	 15,000
II.	Debentures Suspense A/c Dr. To Debentures A/c (Issue of debentures as collateral security)		25,000	 25,000

ILLUSTRATION 16.

M Ltd. issued 10,000, 8% debentures of ₹100 each at a premium of 10% on 1-4-2021. It purchased fixed assets of the value of ₹2,50,000 and took over current liabilities of ₹40,000 and issued 8% debentures at a premium of 5% to the vendor. On the same date it took loan from the Bank for ₹1,00,000 and issued 8% debentures as Collateral Security. Record the relevant journal entries in the books of *M* Ltd. and prepare the extract of balance sheet on 31-3-2022. Ignore interest.

SOLUTION :

M. Ltd.

JOURNAL

Date	*Particulars*	*L.F.*	*Dr.*	*Cr.*
2021			₹	₹
April 1	Bank A/c Dr. To 8% Debenture Application & Allotment A/c (Application money received on 10,000 debentures @ ₹110 each)		11,00,000	 11,00,000
April 1	8% Debenture Application & Allotment A/c Dr. To 8% Debentures A/c To Securities Premium Reserve A/c (Transfer of application money to Debentures A/c and Securities Premium Reserve A/c)		11,00,000	 10,00,000 1,00,000
April 1	Fixed Assets A/c Dr. To Current Liabilities A/c To Vendor's A/c (Purchase of assets and liabilities)		2,50,000	 40,000 2,10,000

April 1	Vendor's A/c Dr. To 8% Debentures A/c To Securities Premium Reserve A/c (Issue of 2,000 debentures of ₹100 each at 5% premium calculated as follows : $\frac{2,10,000}{105} = 2,000$ debentures)		2,10,000	 2,00,000 10,000
April 1	Bank A/c Dr. To Bank Loan A/c (Loan taken, secured by the issue of ₹1,00,000 debentures)		1,00,000	 1,00,000
April 1	8% Debentures Suspense A/c Dr. To 8% Debentures A/c (Issue of debentures as collateral security)		1,00,000	 1,00,000

EXTRACT OF BALANCE SHEET

as at 31st March, 2022

Particulars	*Note No.*	*Current Year*	*Previous Year*
I. EQUITY AND LIABILITIES		₹	₹
Shareholder's Funds :			
Reserve and Surplus	1	1,10,000	
Non-Current Liabilities :			
Long-term Borrowings	2	13,00,000	
Current Liabilities		40,000	
II. ASSETS			
Non-Current Assets :			
Fixed Assets		2,50,000	

Notes to Accounts :

		₹
(1) **Reserve and Surplus :**		
Securities Premium Reserve		1,10,000
(2) **Long-term Borrowings :**		
8% Debentures	13,00,000	
Less : Debenture Suspense A/c	1,00,000	12,00,000
Bank Loan (On Collateral Security of Debentures ₹1,00,000)		1,00,000
		13,00,000

Redemption of Debentures

Debentures are the liabilities of the Company. The repayment of debentures is called the redemption of debentures. The repayment of debentures is made by the Company in accordance with the terms of issue, as stated in the prospectus.

Following entries are passed for the redemption of debentures :

Debentures A/c	Dr.
To Debentureholders A/c	
Debentureholders A/c	Dr.
To Bank A/c	

Accounting for Issue of Debentures Considering the Terms and Conditions of Redemption

Debentures may be redeemed either at par or at premium, according to the terms laid down at the time of issue. After taking into account the three possibilities of issue (*i.e.*, at par, at discount, at premium) and two possibilities of redemption (*i.e.*, at par or at premium) a Company can issue debentures from the following six types :

1. **When debentures are issued at par and are redeemable at par** : For example, if a debenture of ₹100 is issued at ₹100 and is redeemable at ₹100, the following entries will be passed :

Entries for Issue :				**Entries for Redemption :**			
Bank A/c	Dr.	100		Debentures A/c	Dr	100	
To Debenture Application & Allotment A/c			100	To Debentureholders A/c			100
Debenture Application & Allotment A/c	Dr.	100		Debentureholders A/c	Dr.	100	
To Debentures A/c			100	To Bank A/c			100

2. **When debentures are issued at a discount and are redeemable at par** : For example, if a debenture of ₹100 is issued at ₹95 and is redeemable at ₹100, the following entries will be passed :

Entries for Issue :				**Entries for Redemption :**			
Bank A/c	Dr.	95		Debentures A/c	Dr.	100	
To Debenture Application & Allotment A/c			95	To Debentureholders A/c			100
Debenture Application & Allotment A/c	Dr.	95		Debentureholders A/c	Dr.	100	
Discount on Issue of Debentures A/c	Dr.	5		To Bank A/c			100
To Debentures A/c			100				

3. **When debentures are issued at a premium and are redeemable at par** : For example, if a debenture of ₹100 is issued at ₹105 and is redeemable at ₹100, the following entries will be passed :

Entries for Issue :				**Entries for Redemption :**			
Bank A/c	Dr.	105		Debentures A/c	Dr.	100	
To Debenture Application & Allotment A/c			105	To Debentureholders A/c			100

Debenture Application & Allotment A/c	Dr.	105		Debentureholders A/c Dr.	100	
To Debentures A/c			100	To Bank A/c		100
To Securities Premium Reserve A/c			5			

Securities Premium Reserve A/c has a credit balance and is a capital profit, to be shown on the equity and liabilities side under the head, "Reserves and Surplus".

4. **When debentures are issued at par and are redeemable at a premium :** Sometimes the debentures are issued with the specific condition that the Company will pay a premium at the time of their redemption. Although, such premium will be paid at the time of actual redemption, but as it is a known loss, the Company records such loss at the time of issue by debiting an account called, "Loss on issue of debentures A/c". It is done in keeping with the convention of conservatism.

For example, if a debenture of ₹100 is issued at ₹100 and is redeemable at ₹105, the following entries will be passed :

Entries for Issue :				**Entries for Redemption :**			
Bank A/c	Dr.	100		Debentures A/c	Dr.	100	
To Debenture Application & Allotment A/c			100	Premium on Redemption of Debentures A/c	Dr.	5	
Debenture Application & Allotment A/c	Dr.	100		To Debentureholders A/c			105
Loss on Issue of Debentures A/c	Dr.	5		Debentureholders A/c	Dr.	105	
To Debentures A/c			100	To Bank A/c			105
To Premium on Redemption of Debentures A/c			5				

'Loss on issue of debentures A/c' is a loss on account of promise to pay debentures at premium at the time of their redemption. This is a capital loss and is written off in the same year or during the tenure of debentures just like discount on debentures. The entry for writing off will be :

Statement of Profit and Loss Dr.
To Loss on Issue of Debentures A/c

'Premium on Redemption of Debentures A/c' shows a credit balance. It is a liability on the part of the Company and appears under the head : 'Non-Current Liabilities' under sub-head 'Long term Borrowings' on the equity and liability side of the balance sheet each year, until the debentures are repaid. At the time of redemption of debentures, this account is debited and closed off.

5. **When debentures are issued at a discount and are redeemable at a premium:** For example, if a debenture of ₹100 is issued at ₹98 and is redeemable at ₹105, the following entries will be passed :

Entries for Issue :				**Entries for Redemption :**			
Bank A/c	Dr.	98		Debentures A/c	Dr.	100	
To Debenture Application & Allotment A/c			98	Premium on Redemption of Debentures A/c	Dr.	5	

Debenture Application & Allotment A/c Dr.	98		To Debentureholders A/c		105
Loss on Issue of Debentures A/c Dr.	7		Debentureholders A/c Dr.	105	
To Debentures A/c		100	To Bank A/c		105
To Premium on Redemption of Debentures A/c		5			

Both, the amount of discount allowed ₹2 and premium on redemption ₹5 are capital losses and therefore, grouped together and debited to 'Loss on issue' as ₹7.

6. **When debentures are issued at premium and are redeemable at a premium:** For example, if a debenture of ₹100 is issued at ₹106 and is redeemable at ₹110, the following entries will be passed :

Entries for Issue :			**Entries for Redemption :**		
Bank A/c Dr.	106		Debentures A/c Dr.	100	
To Debenture Application & Allotment A/c		106	Premium on Redemption of Debentures A/c Dr.	10	
Debenture Application & Allotment A/c Dr.	106		To Debentureholders A/c		110
Loss on Issue of Debentures A/c Dr.	10		Debentureholders A/c Dr.	110	
To Debentures A/c		100	To Bank A/c		110
To Securities Premium Reserve A/c		6			
To Premium on Redemption of Debentures A/c		10			

On the equity & liabilities side, securities premium reserve will be shown under the head "Reserves and Surplus" and Premium on Redemption will be shown under the head "Non-Current Liabilities" under the sub-head 'Long term Borrowings'.

Note : Debentures cannot be redeemed at discount, although a Company may redeem its debentures by purchasing them in the open market at a discount.

ILLUSTRATION 17.

Give journal entries for the issue of debentures in the following conditions. Also prepare the Balance Sheet in each case :

I. Issued 2,000, 12% debentures of ₹100 each at par, redeemable also at par.

II. Issued 2,000, 12% debentures of ₹100 each at a discount of 2%, redeemable at par.

III. Issued 2,000, 12% debentures of ₹100 each at a premium of 5%, redeemable at par.

IV. Issued 2,000, 12% debentures of ₹100 each at par but redeemable at 5% premium.

V. Issued 2,000, 12% debentures of ₹100 each at a discount of 2%, redeemable at a premium of 5%.

VI. Issued 2,000, 12% debentures of ₹100 each at a premium of 5%, redeemable at a premium of 10%.

Assume that the discount or loss on issue is to be written off in the first year itself.

SOLUTION : I.

JOURNAL

Date	*Particulars*	*L.F.*	*Dr.*	*Cr.*
			₹	₹
	Bank A/c Dr.		2,00,000	
	To 12% Debenture Application & Allotment A/c			2,00,000
	(Application money received)			
	12% Debenture Application & Allotment A/c Dr.		2,00,000	
	To 12% Debentures A/c			2,00,000
	(Transfer of application money to Debentures Account, issued at par)			

BALANCE SHEET OF

.... *as at*.... .. ..

Particulars	*Note No.*	*Current Year*	*Previous Year*
I. EQUITY AND LIABILITIES		₹	₹
Non-current Liabilities :			
Long-term Borrowings	1	2,00,000	
II. ASSETS			
Current Assets :			
Cash and Bank Balance	2	2,00,000	

Notes to Accounts :

	₹
(1) **Long-term Borrowings :**	
2,000, 12% Debentures of ₹100 each	2,00,000
(2) **Cash and Bank Balance :**	
Cash at Bank	2,00,000

II.

JOURNAL

Date	*Particulars*	*L.F.*	*Dr.*	*Cr.*
			₹	₹
	Bank A/c Dr.		1,96,000	
	To 12% Debenture Application & Allotment A/c			1,96,000
	(Application money received)			
	12% Debenture Application & Allotment A/c Dr.		1,96,000	
	Discount on issue of Debentures A/c Dr.		4,000	
	To 12% Debentures A/c			2,00,000
	(Transfer of application money to Debentures Account, issued at a discount of 2%)			

BALANCE SHEET OF .... *as at*...............

Particulars	*Note No.*	*Current Year* ₹	*Previous Year* ₹
I. EQUITY AND LIABILITIES			
Shareholder's Funds :			
Reserve and Surplus	1	(4,000)*	
Non-Current Liabilities :			
Long-term Borrowings	2	2,00,000	
		1,96,000	
II. ASSETS			
Current Assets :			
Cash and Bank Balance	3	1,96,000	

Notes to Accounts :

	₹
(1) **Reserves and Surplus :**	
Balance in Statement of Profit and Loss (Discount on Issue of Debentures)	(4,000)*
(2) **Long-term Borrowings :**	
2,000, 12% Debentures of ₹100 each	2,00,000
(3) **Cash and Bank Balance :**	
Cash at Bank	1,96,000

* It represents negative balance in Statement of Profit and Loss.

III. JOURNAL

Date	*Particulars*		*L.F.*	*Dr.* ₹	*Cr.* ₹
	Bank A/c	Dr.		2,10,000	
	To 12% Debenture Application & Allotment A/c				2,10,000
	(Application money received)				
	12% Debenture Application & Allotment A/c	Dr.		2,10,000	
	To 12% Debentures A/c				2,00,000
	To Securities Premium Reserve A/c				10,000
	(Transfer of application money to Debentures Account, issued at a premium of 5%)				

BALANCE SHEET OF

.... *as at*...............

Particulars	*Note No.*	*Current Year* ₹	*Previous Year* ₹
I. EQUITY AND LIABILITIES			
Shareholder's Funds :			
Reserve and Surplus	1	10,000	

Non-Current Liabilities :			
Long-term Borrowings	2	2,00,000	
		2,10,000	
II. ASSETS			
Current Assets :			
Cash and Bank Balance	3	2,10,000	

Notes to Accounts :

	₹
(1) **Reserves and Surplus :**	
Securities Premium Reserve	10,000
(2) **Long-term Borrowings :**	
2,000, 12% Debentures of ₹100 each	2,00,000
(3) **Cash and Bank Balance :**	
Cash at Bank	2,10,000

IV. JOURNAL

Date	*Particulars*		*L.F.*	*Dr.*	*Cr.*
				₹	₹
	Bank A/c	Dr.		2,00,000	
	To 12% Debenture Application & Allotment A/c				2,00,000
	(Application money received)				
	12% Debenture Application & Allotment A/c	Dr.		2,00,000	
	Loss on issue of debentures A/c	Dr.		10,000	
	To 12% Debentures A/c				2,00,000
	To Premium on Redemption A/c				10,000
	(Transfer of application money to Debentures Account, issued at par, but redeemable at a premium of 5%)				

BALANCE SHEET OF................

as at...............

Particulars	*Note No.*	*Current Year*	*Previous Year*
		₹	₹
I. EQUITY AND LIABILITIES			
Shareholder's Funds :			
Reserve and Surplus	1	(10,000)	
Non-Current Liabilities :			
Long-term Borrowings	2	2,10,000	
		2,00,000	
II. ASSETS			
Current Assets :			
Cash and Bank Balance	3	2,00,000	

Notes to Accounts :

	₹
(1) **Reserves and Surplus :**	
Balance in Statement of Profit & Loss (Loss on Issue of Debentures)	(10,000)
(2) **Long-term Borrowings :**	
2,000, 12% Debentures of ₹100 each	2,00,000
Premium on Redemption	10,000
	2,10,000
(3) **Cash and Bank Balance :**	
Cash at Bank	2,00,000

V. JOURNAL

Date	*Particulars*	*L.F.*	*Dr.*	*Cr.*
			₹	₹
	Bank A/c Dr.		1,96,000	
	To 12% Debenture Application & Allotment A/c			1,96,000
	(Application money received)			
	12% Debenture Application & Allotment A/c Dr.		1,96,000	
	Loss on issue of debentures A/c(1) Dr.		14,000	
	To 12% Debentures A/c			2,00,000
	To Premium on Redemption A/c			10,000
	(Transfer of application money to Debentures Account, issued at a discount of 2% and redeemable at a premium of 5%)			

Note 1 : Loss on issue A/c has been debited by ₹14,000 by grouping together the discount on issue ₹4,000 and premium on redemption ₹10,000.

BALANCE SHEET OF................

as at..............

Particulars	*Note No.*	*Current Year*	*Previous Year*
I. EQUITY AND LIABILITIES		₹	₹
Shareholder's Funds :			
Reserve and Surplus	1	(14,000)	
Non-Current Liabilities :			
Long-term Borrowings	2	2,10,000	
		1,96,000	
II. ASSETS			
Current Assets :			
Cash and Bank Balance	3	1,96,000	

Notes to Accounts :

	₹
(1) Reserves and Surplus :	
Balance in Statement of Profit & Loss (Loss on Issue of Debentures)	(14,000)
(2) Long-term Borrowings :	
2,000, 12% Debentures of ₹100 each	2,00,000
Premium on Redemption	10,000
	2,10,000
(3) Cash and Bank Balance :	
Cash at Bank	1,96,000

VI. JOURNAL

Date	*Particulars*		*L.F.*	*Dr.*	*Cr.*
				₹	₹
	Bank A/c	Dr.		2,10,000	
	To 12% Debenture Application & Allotment A/c				2,10,000
	(Application money received)				
	12% Debenture Application & Allotment A/c	Dr.		2,10,000	
	Loss on issue of debentures A/c	Dr.		20,000	
	To 12% Debentures A/c				2,00,000
	To Securities Premium Reserve A/c				10,000
	To Premium on Redemption A/c				20,000
	(Transfer of application money to Debentures Account, issued at a premium of 5% and redeemable at a premium of 10%)				

BALANCE SHEET OF................

as at...............

Particulars	*Note No.*	*Current Year*	*Previous Year*
I. EQUITY AND LIABILITIES :		₹	₹
Shareholder's Funds :			
Reserve and Surplus	1	(10,000)	
Non-Current Liabilities :			
Long-term Borrowings	2	2,20,000	
		2,10,000	
II. ASSETS :			
Current Assets :			
Cash and Bank Balance	3	2,10,000	

Notes to Accounts :

	₹
(1) Reserves and Surplus :	
Securities Premium Reserve	10,000
Loss on Issue of Debentures	(20,000)
	(10,000)
(2) Long-term Borrowings :	
2,000, 12% Debentures of ₹100 each	2,00,000
Premium on Redemption	20,000
	2,20,000
(3) Cash and Bank Balance :	
Cash at Bank	2,10,000

ILLUSTRATION 18.

You are required to pass journal entries to record the following issues of debentures and to write off any capital losses.

(*a*) Zoom Ltd. issues 6,000, 12% Debentures of ₹100 each at par redeemable after 5 years also at par.

(*b*) Zola Ltd. issues 5,000, 13% Debentures of ₹100 each at a discount of 10% to be redeemed at par after 7 years.

(*c*) Zubic Ltd. issues 11% Debentures of the total face value of ₹12,00,000 at a premium of 5% to be redeemed at par after 6 years.

(*d*) Ruby Ltd. issues ₹5,00,000, 12% Debentures at a premium of 5% to be redeemed at 10% premium after 10 years.

(*e*) Emerald Ltd. issues 3,000, 9% Debentures of ₹100 each at a discount of 7%, to be redeemed at a premium of 10% after 4 years.

Note : All the companies write off their capital losses in the year in which they occur.

(I.S.C. 2019)

SOLUTION :

(*a*) JOURNAL OF ZOOM LTD.

Date	*Particulars*	*L.F.*	*Dr. (₹)*	*Cr. (₹)*
	Bank A/c Dr.		6,00,000	
	To Debenture Application & Allotment A/c			6,00,000
	(Debenture Application & Allotment money received)			
	Debenture Application & Allotment A/c Dr.		6,00,000	
	To 12% Debentures A/c			6,00,000
	(6,000 debentures issued at par, redeemable at par)			

(*b*) JOURNAL OF ZOLA LTD.

Date	*Particulars*	*L.F.*	*Dr. (₹)*	*Cr. (₹)*
	Bank A/c Dr.		4,50,000	
	To Debenture Application & Allotment A/c			4,50,000
	(Debenture Application & Allotment money received)			

	Debenture Application & Allotment A/c Dr.		4,50,000	
	Discount on Issue of Debentures A/c Dr.		50,000	
	To 13% Debentures A/c			5,00,000
	(5,000 Debentures issued at discount, to be redeemed at par)			
	Statement of Profit & Loss Dr.		50,000	
	To Discount on Issue of Debentures A/c			50,000
	(Discount on Debentures written off)			

(*c*) JOURNAL OF ZUBIC LTD.

Date	*Particulars*	*L.F.*	*Dr.* (₹)	*Cr.* (₹)
	Bank A/c Dr.		12,60,000	
	To Debenture Application & Allotment A/c			12,60,000
	(Debenture Application & Allotment money received)			
	Debenture Application & Allotment A/c Dr.		12,60,000	
	To 11% Debentures A/c			12,00,000
	To Securities Premium Reserve A/c			60,000
	(12,000 Debentures issued at premium, to be redeemed at par)			

(*d*) JOURNAL OF RUBY LTD.

Date	*Particulars*	*L.F.*	*Dr.* (₹)	*Cr.* (₹)
	Bank A/c Dr.		5,25,000	
	To Debenture Application & Allotment A/c			5,25,000
	(Debenture Application & Allotment money received)			
	Debenture Application & Allotment A/c Dr.		5,25,000	
	Loss on Issue of Debentures A/c Dr.		50,000	
	To 12% Debentures A/c			5,00,000
	To Securities Premium Reserve A/c			25,000
	To Premium on Redemption of Debentures A/c			50,000
	(5,000 Debentures issued at premium to be redeemed at premium)			
	Securities Premium Reserve A/c Dr.		25,000	
	Statement of Profit & Loss Dr.		25,000	
	To Loss on Issue of Debentures A/c			50,000
	(Loss on issue of Debentures written off)			

(*e*) JOURNAL OF EMERALD LTD.

Date	*Particulars*	*L.F.*	*Dr.* (₹)	*Cr.* (₹)
	Bank A/c Dr.		2,79,000	
	To Debenture Application & Allotment A/c			2,79,000
	(Debenture Application & Allotment money received)			

Debenture Application & Allotment A/c	Dr.	2,79,000	
Loss on Issue of Debentures A/c(1)	Dr.	51,000	
To 9% Debentures A/c			3,00,000
To Premium on Redemption of Debentures A/c			30,000
(3,000 Debentures issued at discount to be redeemed at premium)			
Statement of Profit & Loss	Dr.	51,000	
To Loss on Issue of Debentures A/c			51,000
(Loss on issue of Debentures written off)			

Note (1) : Loss on Issue of Debentures A/c has been debited by ₹51,000 by grouping together the discount on issue ₹21,000 and premium on redemption ₹30,000.

Interest on Debentures

Interest on debentures is usually paid half-yearly. Interest on debentures is a charge against the profits of the Company. It has to be paid regularly even if the Company suffers a loss or does not earn profit. The rate of interest payable on debentures is prefixed on debentures. For example, if the rate of interest is 9% p.a., the name given to debentures will be '9% debentures'. As per Income Tax Act, a Company is required to deduct income tax at the prescribed rate from the gross amount of debenture interest before any amount is paid to the debentureholders. The tax thus deducted is to be deposited in Government Account on behalf of the debentureholders.

While preparing the final accounts for an accounting period, provision must be made for any accrued interest on the very date of preparing the balance sheet. Accrued interest may be of two types :

I. **Interest accrued and due** : If a Company pays interest on debentures half-yearly on 30th June and 31st December, while preparing the balance sheet on 31st March, 2022, if the interest for the period ending 31st Dec., 2021 remains unpaid, it will be called 'Interest accrued and due'.

II. **Interest accrued but not due** : If a Company pays interest on debentures half-yearly on 30th June and 31st December, while preparing the balance sheet on 31st March, 2022, the interest for the period from 1st January 2022 to 31st March, 2022 will be called 'Interest accrued but not due'.

Both the types of accrued interest as discussed above, will be shown on the liabilities side of the balance sheet.

Following entries are passed for interest on debentures :

1. When interest is due and tax is deducted at source (TDS) :

Interest on Debentures A/c	Dr.
To Debentureholders A/c	
To TDS Payable A/c	
(Interest due to debentureholders and tax deducted at source)	

2. When interest is paid to the debentureholders :

Debentureholders A/c	Dr.
To Bank A/c	
(Payment of interest)	

3. On payment of tax deducted at source :

TDS Payable A/c Dr.
To Bank A/c
(Depositing the amount of TDS in Government Account)

4. On transfer of debenture interest to Statement of Profit and Loss at the end of the year :

Statement of Profit & Loss Dr.
To Interest on Debentures A/c
(Interest transferred to Statement of P & L)

ILLUSTRATION 19.

On 1.4.2015, J.K. Ltd. issued 8,000, 9% debentures of ₹1,000 each at a discount of 6%, redeemable at a premium of 5% after three years. The company closes its books on 31st March every year. Interest on 9% debentures is payable on 30th September and 31st March every year. The rate of tax deducted at source is 10%.

Pass necessary journal entries for the issue of debentures and debenture interest for the year ended 31.3.2016. *(C.B.S.E. 2017, Outside Delhi)*

SOLUTION :

JOURNAL OF J.K. LTD.

Date	*Particulars*		*L.F.*	*Dr. (₹)*	*Cr. (₹)*
2015					
April 1	Bank A/c	Dr.		75,20,000	
	To Debenture Application & Allotment A/c				75,20,000
	(Amount received on application)				
April 1	Debenture Application & Allotment A/c	Dr.		75,20,000	
	Loss on Issue of Debentures A/c	Dr.		8,80,000	
	To 9% Debentures A/c				80,00,000
	To Premium on Redemption of Debentures A/c				4,00,000
	(Issue of Debentures at 6% discount and redeemable at 5% premium)				
Sept. 30	Interest on Debentures A/c	Dr.		3,60,000	
	To Debentureholders A/c				3,24,000
	To TDS Payable A/c				36,000
	(Half-yearly interest due on debentures and tax deducted at source)				
Sept. 30	Debentureholders A/c	Dr.		3,24,000	
	To Bank A/c				3,24,000
	(Payment of interest)				
Sept. 30	TDS Payable A/c	Dr.		36,000	
	To Bank A/c				36,000
	(TDS deposited in Government Account)				

2016 March 31	Interest on Debentures A/c To Debentureholders A/c To TDS Payable A/c (Half-yearly interest due on debentures and tax deducted at source)	Dr.	3,60,000	 3,24,000 36,000
March 31	Debentureholders A/c To Bank A/c (Payment of interest)	Dr.	3,24,000	 3,24,000
March 31	TDS Payable A/c To Bank A/c (TDS deposited in Government Account)	Dr.	36,000	 36,000
March 31	Statement of Profit & Loss To Interest on Debentures A/c (₹3,60,000 + ₹3,60,000) (Interest transferred to Statement of Profit and Loss)	Dr.	7,20,000	 7,20,000

Writing off Discount/Loss on Issue of Debentures

Discount/Loss on issue of debentures is a capital loss to the Company. It must be written off before such debentures are redeemed. Section 52 of the Companies Act, 2013 allows the utilisation of securities premium for writing off the discount or loss on issue of debentures. Until the discount or loss on Issue is written off, it is required to be shown as Unamortized Expenses on the Assets side of the Balance Sheet. Following entry is passed to write off the discount on debentures :

Statement of Profit & Loss Dr.
To Discount/Loss on issue of Debentures A/c

Discount or Loss on issue of debentures can be written off following any of the following two options :

(*i*) It may be written off in the first year itself; or

(*ii*) It may be written off during the tenure (life) of the debentures.

(*i*) Discount or Loss on issue may be written off in the first year itself, first from Securities Premium Reserve or from Capital Reserve or from Statement of Profit and Loss in that order.

The entry will be :

Security Premium Reserve A/c Dr.
and/or
Capital Reserve A/c Dr.
and/or
Statement of Profit and Loss Dr.
To Discount or Loss on Issue of Debentures A/c

ILLUSTRATION 20.

On 1-4-2021, Fast Computers Ltd. issued 20,000, 6% debentures of ₹100 each at a discount of 4% redeemable at a premium of 5% after three years. The amount was payable as follows :

On application ₹50 per debenture.

Balance on allotment.

Fast Computers has a balance of ₹50,000 in Securities Premium Reserve and ₹1,00,000 in Capital Reserve. Profit for the year was ₹75,000. Company decided to write off the entire loss on issue of debentures in the first year itself.

Pass the journal entries for issue of debentures and writing off the loss on issue of debentures and prepare an extract of Balance Sheet as at 31st March 2022, showing the relevant items.

SOLUTION :

Books of Fast Computers Ltd.

JOURNAL

Date	Particulars		L.F.	Dr.	Cr.
2021				₹	₹
April 1	Bank A/c	Dr.		10,00,000	
	To 6% Debenture Application A/c				10,00,000
	(Receipt of application money on 20,000 debentures @ ₹50 each)				
April 1	6% Debenture Application A/c	Dr.		10,00,000	
	To 6% Debentures A/c				10,00,000
	(Application money transferred to 6% Debentures Account)				
April 1	6% Debenture Allotment A/c	Dr.		9,20,000	
	Loss on issue of Debentures A/c	Dr.		1,80,000	
	To 6% Debentures A/c				10,00,000
	To Premium on Redemption A/c				1,00,000
	(Amount due @ ₹46 each on 20,000 debentures issued at 4% discount and redeemable at 5% premium)				
April 1	Bank A/c	Dr.		9,20,000	
	To 6% Debenture Allotment A/c				9,20,000
	(Allotment money received)				
2022					
March 31	Securities Premium Reserve A/c	Dr.		50,000	
	Capital Reserve A/c	Dr.		1,00,000	
	Statement of Profit & Loss	Dr.		30,000	
	To Loss on Issue of Debentures A/c				1,80,000
	(Loss on Issue of Debentures written off)				

An Extract of Balance Sheet

as at 31st March, 2022

Particulars	Note No.	Current Year	Previous Year
I. EQUITY AND LIABILITIES :		₹	₹
Shareholder's Funds :			
Reserves and Surplus	1	45,000	

Non-Current Liabilities : Long-term Borrowings	2	21,00,000	

Notes to Accounts :

		₹
(1) Reserves and Surplus :		
Securities Premium Reserve	50,000	
Less : Loss on Issue of Debentures	50,000	—
Capital Reserve	1,00,000	
Less : Loss on Issue of Debentures	1,00,000	—
Surplus i.e. Balance in Statement of Profit & Loss (₹75,000 - ₹30,000)		45,000
(2) Long-term Borrowings :		
20,000, 6% Debentures of ₹100 each		20,00,000
Premium on Redemption		1,00,000
		21,00,000

ILLUSTRATION 21.

Sh. Ganesh Ltd. issued on 1st April, 2018, 10,000, 8% Debentures of ₹100 each at 6% discount redeemable after five years at a premium of ₹10. All the debentures were subscribed. During the year ended 31st March, 2019, the company incurred a loss of ₹50,000. It has balance of ₹1,20,000 in Securities Premium Reserve. Company decided to write off the loss on issue of debentures in the first year itself.

Pass the Journal entries for issue of debentures and prepare the extract of the Balance Sheet showing Loss on Issue of Debentures.

SOLUTION :

JOURNAL OF SH. GANESH LTD.

Date	*Particulars*		*L.F.*	*Dr.*	*Cr.*
2018				₹	₹
April 1	Bank A/c	Dr.		9,40,000	
	To Debentures Application and Allotment A/c				9,40,000
	(Application money received for 10,000, 8% Debentures)				
April 1	Debentures Application and Allotment A/c	Dr.		9,40,000	
	Loss on Issue of Debentures A/c	Dr.		1,60,000	
	To 8% Debentures A/c				10,00,000
	To Premium on Redemption of Debentures A/c				1,00,000
	(Transfer of application money)				
2019					
March 31	Securities Premium Reserve A/c	Dr.		1,20,000	
	Statement of Profit and Loss	Dr.		40,000	
	To Loss on Issue of Debentures A/c				1,60,000
	(Loss on issue of Debentures written off)				

BALANCE SHEET (EXTRACT)
as at 31st March, 2019

Particulars	*Note No.*	*Current Year*	*Previous Year*
I. EQUITY AND LIABILITIES :		₹	₹
Shareholder's Funds :			
Reserves and Surplus	1	(90,000)	

Notes to Accounts :

	₹	₹
(1) **Reserves and Surplus :**		
Securities Premium Reserve	1,20,000	
Less : Loss on Issue of Debentures Written off	1,20,000	—
Surplus, i.e., Balance in Statement of Profit and Loss (–₹50,000 – ₹40,000)		(90,000)
		(90,000)

ILLUSTRATION 22.

On 1st April, 2021, Alok Ltd. issued 7,000, 10% Debentures of ₹500 each at a premium of 5% and redeemable at a premium of 10% after 5 years. According to the terms of issue, ₹200 was payable on application and balance on allotment. Record necessary entries regarding issue of debentures. Entire loss on issue of debentures is to be written off in the first year.

SOLUTION :

Alok Ltd.
JOURNAL

Date	*Particulars*		*L.F.*	*Dr.*	*Cr.*
2021				₹	₹
April 1	Bank A/c	Dr.		14,00,000	
	To 10% Debenture Application A/c				14,00,000
	(Application money received on 7,000 Debentures @ ₹200 each)				
April 1	10% Debenture Application A/c	Dr.		14,00,000	
	To 10% Debentures A/c				14,00,000
	(Application money adjusted)				
April 1	10% Debenture Allotment A/c	Dr.		22,75,000	
	Loss on Issue of Debentures A/c	Dr.		3,50,000	
	To 10% Debentures A/c				21,00,000
	To Securities Premium Reserve A/c				1,75,000
	To Premium on Redemption of Debentures A/c				3,50,000
	(Allotment money due on 7,000 Debentures @ ₹325 per debenture including premium of ₹25 each and redeemable at 10% premium)				
April 1	Bank A/c	Dr.		22,75,000	
	To 10% Debenture Allotment A/c				22,75,000
	(Allotment money received)				

2022 March 31	Securities Premium Reserve A/c Dr. Statement of Profit & Loss Dr. To Loss on Issue of Debentures A/c (Loss on issue of debentures written off)		1,75,000 1,75,000	3,50,000

(*ii*) Discount or Loss on issue may also be written off during the tenure (life) of the debentures either by

(*a*) Writing off equal amount each year; or

(*b*) Writing off proportionate amount each year.

(*a*) **Writing off equal amount each year** : When the debentures are to be redeemed after a fixed period in lump sum, the total amount of discount or loss on issue should be spread over the lifetime of debentures equally. For example, if the debentures amounting to ₹10,00,000 are issued at a discount of 6%, repayable at the end of five years, then :

Total Discount = 6% of ₹10,00,000 = ₹60,000

Amount of discount to be written off each year from Statement of P & L = $\frac{60,000}{5}$

= ₹12,000.

ILLUSTRATION 23.

On 1st April, 2015, a Limited Company issued 11% ₹10,00,000 debentures at a discount of 6%, repayable at the end of 5 years at par. Pass journal entries for the issue of debentures and prepare Discount on Issue of Debentures Account for five years. Assume that the accounts are closed on 31st March each year.

SOLUTION : JOURNAL ENTRIES FOR ISSUE OF DEBENTURES

Date	*Particulars*	*L.F.*	*Dr.* (₹)	*Cr.* (₹)
2015 April 1	Bank A/c Dr. To 11% Debenture Application & Allotment A/c (Receipt of application money on debentures)		9,40,000	9,40,000
April 1	11% Debenture Application & Allotment A/c Dr. Discount on Issue of Debentures A/c Dr. To 11% Debentures A/c (Issue of Debentures at 6% discount and redeemable at par)		9,40,000 60,000	10,00,000

Dr. DISCOUNT ON ISSUE OF DEBENTURES A/C Cr.

Date	*Particulars*	₹	*Date*	*Particulars*	₹
2015 April 1	To 11% Debentures A/c	60,000	2016 March 31	By Statement of P & L (1/5 of ₹60,000)	12,000

			March 31	By Balance c/d	48,000
		60,000			60,000
2016			2017		
April 1	To Balance b/d	48,000	March 31	By Statement of P & L	12,000
			March 31	By Balance c/d	36,000
		48,000			48,000
2017			2018		
April 1	To Balance b/d	36,000	March 31	By Statement of P & L	12,000
			March 31	By Balance c/d	24,000
		36,000			36,000
2018			2019		
April 1	To Balance b/d	24,000	March 31	By Statement of P & L	12,000
			March 31	By Balance c/d	12,000
		24,000			24,000
2019			2020		
April 1	To Balance b/d	12,000	March 31	By Statement of P & L	12,000
		12,000			12,000

(*b*) **Writing off proportionate amount each year** : When the debentures are redeemed by instalments, the discount or loss on issue of debentures should be written off in the ratio in which the amount of debentures has been used. For example, if the debentures of ₹5,00,000 have been issued at 6% discount and the debentures of ₹1,00,000 are repayable each year, the amount of discount will be written off each year in the ratio of debentures outstanding at the beginning of each year. In this case the amount of discount transferred to Statement of Profit and Loss will be in the ratio of 5,00,000 : 4,00,000 : 3,00,000 : 2,00,000 : 1,00,000. The reason is, that, in the first year the Company has utilised larger amount of funds, *i.e.*, ₹5,00,000 in the business, whereas, in the subsequent years it has used lesser amount of funds, *i.e.*, ₹4,00,000, ₹3,00,000, ₹2,00,000 and ₹1,00,000 respectively. As such, the amount of discount transferred to Statement of Profit & Loss will be in the ratio of 5 : 4 : 3 : 2 : 1.

ILLUSTRATION 24.

A company issued 10,000, 8% Debentures of ₹100 each at a discount of 6% on 1st April, 2015. These debentures are redeemable by annual drawings of ₹2,00,000 made on 31st March each year. The directors decided to write off discount based on the debentures outstanding each year. Prepare Discount on Issue of Debentures account for five years. Also show the relevant items in the Company's Balance Sheet as at 31st March 2016.

SOLUTION :

Total Discount on the issue of debentures = ₹10,00,000 × $\frac{6}{100}$ = ₹60,000.

Since debentures amounting to ₹2,00,000 are to be redeemed each year, the amount of discount written off from Statement of P & L is determined as follows :

Year ending	*Debentures Outstanding*	*Ratio**	*Amount of Discount to be written off each year*		
	₹		₹		₹
31st March 2016	10,00,000	5 or 5/15	60,000 × 5/15	=	20,000
31st March 2017	8,00,000	4 or 4/15	60,000 × 4/15	=	16,000
31st March 2018	6,00,000	3 or 3/15	60,000 × 3/15	=	12,000
31st March 2019	4,00,000	2 or 2/15	60,000 × 2/15	=	8,000
31st March 2020	2,00,000	1 or 1/15	60,000 × 1/15	=	4,000
		15			60,000

*Ratio has been obtained by dividing Debentures Outstanding by 2,00,000.

Dr. DISCOUNT ON ISSUE OF DEBENTURES ACCOUNT Cr.

Date	*Particulars*	₹	*Date*	*Particulars*	₹
2015 April 1	To 8% Debentures A/c	60,000	2016 March 31	By Statement of P & L	20,000
			March 31	By Balance c/d	40,000
		60,000			60,000
2016 April 1	To Balance b/d	40,000	2017 March 31	By Statement of P & L	16,000
			March 31	By Balance c/d	24,000
		40,000			40,000
2017 April 1	To Balance b/d	24,000	2018 March 31	By Statement of P & L	12,000
			March 31	By Balance c/d	12,000
		24,000			24,000
2018 April 1	To Balance b/d	12,000	2019 March 31	By Statement of P & L	8,000
			March 31	By Balance c/d	4,000
		12,000			12,000
2019 April 1	To Balance b/d	4,000	2020 March 31	By Statement of P & L	4,000
		4,000			4,000

An Extract of Balance Sheet
as at 31st March, 2016

Particulars	*Note No.*	*Current Year*	*Previous Year*
I. EQUITY AND LIABILITIES :		₹	₹
(*a*) **Shareholder's Funds :**			
Reserves and Surplus	1	(20,000)	

(*b*) **Non-Current Liabilities :**			
Long-term Borrowings	2	10,00,000	
II. ASSETS			
(*a*) **Non-Current Assets**			
Other Non-Current Assets	3	24,000	
(*b*) **Current Assets**			
Other Current Assets	4	16,000	

Notes to Accounts :

		₹
(1) **Reserve and Surplus :**		
Surplus : Balance in Statement of Profit and Loss	—	
Less : Discount on Issue of Debentures written off	(20,000)	(20,000)
(2) **Long-term Borrowings :**		
10,000, 8% Debentures of ₹100 each		10,00,000
(3) **Other Non-Current Assets :**		
Discount on Issue of Debentures	60,000	
Less : Written off from Statement of Profit and Loss	20,000	
	40,000	
Less : To be written off next year	16,000	24,000
(4) **Other Current Assets :**		
Discount on Issue of Debentures (to be written off next year)		16,000

ILLUSTRATION 25.

A Ltd. company issued 9% Debentures of the face value of ₹6,00,000 at a discount of 5% on 1st April, 2014. The debentures are repayable by annual drawing of ₹2,00,000 commencing from the end of 4th year.

Show the 'Discount on Issue of Debentures A/c', in the company's ledger for the period of duration of debentures. Accounts are closed on 31st March each year.

SOLUTION :

$$\text{Total Discount} = 6{,}00{,}000 \times \frac{5}{100} = ₹30{,}000$$

As the first repayment of debentures is made after four years, therefore, the full amount of debentures ₹6,00,000 has been utilised for the first four years. Amount utilised in fifth year amounts to ₹6,00,000 – ₹2,00,000 = ₹4,00,000 and amount utilised in sixth year amounts to ₹4,00,000 – ₹2,00,000 = ₹2,00,000. Hence, the amount of discount transferred to Statement of P & L will be in the ratio of 6,00,000 : 6,00,000 : 6,00,000 : 6,00,000 : 4,00,000 : 2,00,000 *i.e.*, 3 : 3 : 3 : 3 : 2 : 1.

Year	*Amount Utilised* ₹	*Ratio*	*Amount of discount transferred to Statement of P & L* ₹		₹
1	6,00,000	3	30,000 × 3/15	=	6,000
2	6,00,000	3	30,000 × 3/15	=	6,000
3	6,00,000	3	30,000 × 3/15	=	6,000
4	6,00,000	3	30,000 × 3/15	=	6,000
5	4,00,000	2	30,000 × 2/15	=	4,000
6	2,00,000	1	30,000 × 1/15	=	2,000
		15			30,000

DISCOUNT ON ISSUE OF DEBENTURES ACCOUNT

Dr. Cr.

Date	*Particulars*	₹	*Date*	*Particulars*	₹
2014			2015		
April 1	To 9% Debentures A/c	30,000	March 31	By Statement of P & L	6,000
			March 31	By Balance c/d	24,000
		30,000			30,000
2015			2016		
April 1	To Balance b/d	24,000	March 31	By Statement of P & L	6,000
			March 31	By Balance c/d	18,000
		24,000			24,000
2016			2017		
April 1	To Balance b/d	18,000	March 31	By Statement of P & L	6,000
			March 31	By Balance c/d	12,000
		18,000			18,000
2017			2018		
April 1	To Balance b/d	12,000	March 31	By Statement of P & L	6,000
			March 31	By Balance c/d	6,000
		12,000			12,000
2018			2019		
April 1	To Balance b/d	6,000	March 31	By Statement of P & L	4,000
			March 31	By Balance c/d	2,000
		6,000			6,000
2019			2020		
April 1	To Balance b/d	2,000	March 31	By Statement of P & L	2,000
		2,000			2,000

ILLUSTRATION 26.

J Ltd. issued ₹20,00,000, 15% Debentures at 8% discount. Debentures are to be redeemed in the following manner :

Year-end	*Face value of Debentures* ₹
2	2,00,000
3	4,00,000
4	6,00,000
5	8,00,000

Pass journal entry for issue of Debentures and prepare Discount on Issue of Debentures Account for 5 years.

SOLUTION :

Discount allowed on the issue of Debentures $= 20{,}00{,}000 \times \frac{8}{100} =$ ₹1,60,000.

This discount of ₹1,60,000 will be written off from Statement of P & L in the following manner :

Year	*Debentures Outstanding* ₹	*Ratio*	*Amount to be written off* ₹	₹
1	20,00,000	20 or 20/80	1,60,000 × 20/80 =	40,000
2	20,00,000	20 or 20/80	1,60,000 × 20/80 =	40,000
3	18,00,000	18 or 18/80	1,60,000 × 18/80 =	36,000
4	14,00,000	14 or 14/80	1,60,000 × 14/80 =	28,000
5	8,00,000	8 or 8/80	1,60,000 × 8/80 =	16,000
		80		1,60,000

JOURNAL ENTRIES FOR ISSUE OF DEBENTURES

Date	*Particulars*		*L.F.*	*Dr. (₹)*	*Cr. (₹)*
	Bank A/c	Dr.		18,40,000	
	To 15% Debenture Application & Allotment A/c				18,40,000
	(Receipt of application money on debentures)				
	15% Debenture Application & Allotment A/c	Dr.		18,40,000	
	Discount on Issue of Debentures A/c	Dr.		1,60,000	
	To 15% Debentures A/c				20,00,000
	(Transfer of application money to Debentures Account on the issue of debentures at a discount of 8%)				

Dr. DISCOUNT ON ISSUE OF DEBENTURES ACCOUNT Cr.

Year	*Particulars*	₹	*Year*	*Particulars*	₹
I	To 15% Debentures A/c	1,60,000	I	By Statement of P & L	40,000
				By Balance c/d	1,20,000
		1,60,000			1,60,000
II	To Balance b/d	1,20,000	II	By Statement of P & L	40,000
				By Balance c/d	80,000
		1,20,000			1,20,000

III	To Balance b/d	80,000	III	By Statement of P & L By Balance c/d	36,000 44,000
		80,000			80,000
IV	To Balance b/d	44,000	IV	By Statement of P & L By Balance c/d	28,000 16,000
		44,000			44,000
V	To Balance b/d	16,000	V	By Statement of P & L	16,000
		16,000			16,000

ILLUSTRATION 27.

Maneesh Ltd. issued 5,000, 12% debentures of ₹100 each at a discount of 6% to be redeemed as follows :

1st Year : Nil; 2nd Year : ₹2,50,000; 3rd Year : Nil; 4th Year : ₹2,50,000.

Show the Discount on Issue of Debentures Account for the period of 4 years.

SOLUTION :

Discount allowed on issue of Debentures : $5,000 \times 100 \times \frac{6}{100}$ = ₹30,000

It will be written off from Statement of P & L in the following manner :

At the end of	*Debentures Outstanding* ₹	*Ratio*	*Discount to be written off* ₹
1st Year	5,00,000	2	$30,000 \times \frac{2}{6}$ = 10,000
2nd Year	5,00,000	2	$30,000 \times \frac{2}{6}$ = 10,000
3rd Year	2,50,000	1	$30,000 \times \frac{1}{6}$ = 5,000
4th Year	2,50,000	1	$30,000 \times \frac{1}{6}$ = 5,000
		6	30,000

Dr. DISCOUNT ON ISSUE OF DEBENTURES ACCOUNT Cr.

Year	*Particulars*	₹	*Year*	*Particulars*	₹
I	To 12% Debentures A/c	30,000	I	By Statement of P & L By Balance c/d	10,000 20,000
		30,000			30,000
II	To Balance b/d	20,000	II	By Statement of P & L By Balance c/d	10,000 10,000
		20,000			20,000
III	To Balance b/d	10,000	III	By Statement of P & L By Balance c/d	5,000 5,000
		10,000			10,000

IV	To Balance b/d	5,000	IV	By Statement of P & L	5,000
		5,000			5,000

ILLUSTRATION 28.

Ashwathi Ltd. issued 40,000, 10% Debentures of ₹50 each at a discount of 8% on April 1, 2014, redeemable in four equal annual instalments starting with March 31, 2017. Securities premium account shows a balance of ₹70,000. Compute the amount of discount/loss to be written off each year and also record the journal entries in the books of Ashwathi Ltd. Also show the relevant items in the Balance Sheet as at 31st March 2015.

SOLUTION:

		₹
Total Discount = 40,000 × ₹50 × $\frac{8}{100}$	=	1,60,000
Less : Securities Premium	=	70,000
Discount to be written off to Statement of P & L		90,000

Year ending	*Debentures Outstanding* ₹	*Ratio**	*Amount of Discount to be written off to Statement of P & L* ₹ *(in Crores)*
31st March 2015	20,00,000	4	$\frac{4}{18}$ × ₹90,000 = 20,000
31st March 2016	20,00,000	4	$\frac{4}{18}$ × ₹90,000 = 20,000
31st March 2017	20,00,000	4	$\frac{4}{18}$ × ₹90,000 = 20,000
31st March 2018	15,00,000	3	$\frac{3}{18}$ × ₹90,000 = 15,000
31st March 2019	10,00,000	2	$\frac{2}{18}$ × ₹90,000 = 10,000
31st March 2020	5,00,000	1	$\frac{1}{18}$ × ₹90,000 = 5,000
		18	90,000

*Ratio has been obtained by dividing Debentures Outstanding by 5.

Books of Ashwathi Ltd.

JOURNAL

Date	*Particulars*	*L.F.*	*Dr.* ₹	*Cr.* ₹
2014 April 1	Bank A/c Dr. To 10% Debenture Application & Allotment A/c (Application money received)		18,40,000	18,40,000
April 1	10% Debenture Application & Allotment A/c Dr. Discount on Issue of Debentures A/c Dr. To 10% Debentures A/c (Transfer of application money to Debentures Account, issued at a discount of 8%)		18,40,000 1,60,000	20,00,000

2015 March 31	Securities Premium A/c Dr. To Discount on Issue of Debentures A/c (Utilisation of securities premium for writing off discount)	70,000	70,000
March 31	Statement of Profit and Loss Dr. To Discount on Issue of Debentures A/c (Discount written off)	20,000	20,000
2016 March 31	Statement of Profit and Loss Dr. To Discount on Issue of Debentures A/c (Discount written off)	20,000	20,000
2017 March 31	Statement of Profit and Loss Dr. To Discount on Issue of Debentures A/c (Discount written off)	20,000	20,000
2018 March 31	Statement of Profit and Loss Dr. To Discount on Issue of Debentures A/c (Discount written off)	15,000	15,000
2019 March 31	Statement of Profit and Loss Dr. To Discount on Issue of Debentures A/c (Discount written off)	10,000	10,000
2020 March 31	Statement of Profit and Loss Dr. To Discount on Issue of Debentures A/c (Discount written off)	5,000	5,000

An Extract of Balance Sheet
as at 31st March, 2015

Particulars	*Note No.*	*Current Year* ₹	*Previous Year* ₹
I. EQUITY AND LIABILITIES :			
Shareholder's Funds :			
Reserves and Surplus	1	(20,000)	
Non-Current Liabilities :			
Long-term Borrowings	2	20,00,000	
II. ASSETS			
(*a*) **Non-Current Assets**			
Other Non-Current Assets	3	50,000	
(*b*) **Current Assets**			
Other Current Assets	4	20,000	

Notes to Accounts :

		₹
(1) **Reserves and Surplus :**		
Securities Premium Reserve	70,000	
Less : Discount on Issue of Debentures	70,000	—
Surplus : Balance in Statement of Profit & Loss	—	
Less : Discount on Issue of Debentures written off	(20,000)	(20,000)
(2) **Long term Borrowings :**		
40,000, 10% Debentures of ₹50 each		20,00,000
(3) **Other Non-Current Asserts :**		
Discount on Issue of 10% Debentures	1,60,000	
Less : Written off from Security Premium Reserve	70,000	
	90,000	
Less : Written off from Statement of Profit & Loss	20,000	
	70,000	
Less : To be written off next year	20,000	50,000
(4) **Other Current Assets :**		
Discount on Issue of 10% Debentures (to be written off next year		20,000

ILLUSTRATION 29.

Ankur Jewellery Ltd. issued 50,00,000, 8% Debentures of ₹100 each at a discount of 6% on April 1, 2017 redeemable at premium of 4% by draw of lots as under :

20,00,000 Debentures on March 31, 2020

10,00,000 Debentures on March 31, 2021

20,00,000 Debentures on March 31, 2022

Compute the amount of discount to be written off in each year till debentures are paid. Also prepare discount/loss on issue of debentures account.

SOLUTION :

Discount on Issue = ₹50 Crores × $\frac{6}{100}$ = ₹ 3 Crores

Premium on Redemption = ₹50 Crores × $\frac{4}{100}$ = ₹ 2 Crores

Total Loss on Issue of Debentures = ₹ 5 Crores

The loss on issue of debentures will be written off from Statement of P & L in the following manner :

(₹ in Crores)

Year ending	*Debentures Outstanding* ₹	*Ratio**	*Amount of Loss on Issue to be written off to Statement of P & L* ₹	
March 31, 2018	50	5	$\frac{5}{20} \times$ ₹5	1.25

March 31, 2019	50	5	$\frac{5}{20} \times ₹5$ =	1.25
March 31, 2020	50	5	$\frac{5}{20} \times ₹5$ =	1.25
March 31, 2021	30	3	$\frac{3}{20} \times ₹5$ =	0.75
March 31, 2022	20	2	$\frac{2}{20} \times ₹5$ =	0.5
		20		5

*Ratio has been obtained by dividing the debentures outstanding by 10.

LOSS ON ISSUE OF DEBENTURES A/C

Dr. Cr

(₹ in Crores)

Date	Particulars	₹	Date	Particulars	₹
2017			2018		
April 1	To 8% Debentures A/c (6% Discount on 50 Crores)	3	March 31	By Statement of Profit & Loss	1.25
April 1	To Premium on Redemption of Debentures A/c (4% on 50 Crores)	2	March 31	By Balance c/f	3.75
		5			5
2018			2019		
April 1	To Balance b/f	3.75	March 31	By Statement of Profit & Loss	1.25
			March 31	By Balance c/f	2.5
		3.75			3.75
2019			2020		
April 1	To Balance b/f	2.5	March 31	By Statement of Profit & Loss	1.25
			March 31	By Balance c/f	1.25
		2.5			2.5
2020			2021		
April 1	To Balance b/f	1.25	March 31	By Statement of Profit & Loss	0.75
			March 31	By Balance c/f	0.5
		1.25			1.25
2021			2022		
April 1	To Balance b/f	0.5	March 31	By Statement of Profit & Loss	0.5
		0.5			0.5

ISC Examination Questions

ILLUSTRATION 30.

On 1st April, 2013, Relaxo Ltd. purchased assets of ₹5,00,000 and took over liabilities of ₹90,000 of Greg Ltd. at an agreed value of ₹3,80,000. It issued to the vendor, 10% Debentures of ₹100 each at 5% discount, redeemable at par after 5 years, in full satisfaction of the purchase price.

On the same date, the company issued 500, 11% Debentures of ₹100 each as a collateral security to a bank who had advanced a loan of ₹45,000 to it for a period of 3 years and also issued 5,000, 12% Debentures of ₹100 each at par, redeemable after 3 years at 5% premium.

Additional information :

The interest on debentures is paid half yearly on 30th September and 31st March each year. Tax deducted at source @20%. The Company had ₹1,20,000 in its Security Premium Reserve Account which is to be utilized for writing off Loss or Discount on issue of Debentures. (Ignore interest on bank loan)

You are required to show journal entries in the books of Relaxo Ltd. for the year ending 31st March 2014. *(I.S.C. Sample Question Paper 2015)*

SOLUTION : JOURNAL OF RELAXO LTD.

Date	*Particulars*		*L.F.*	*Dr.* (₹)	*Cr.* (₹)
2013 April 1	Sundry Assets A/c	Dr.		5,00,000	
	To Sundry Liabilities A/c				90,000
	To Capital Reserve A/c				30,000
	To Greg Ltd.				3,80,000
	(Purchase of assets and liabilities of Greg Ltd.)				
April 1	Greg Ltd.	Dr.		3,80,000	
	Discount on Issue of Debentures A/c	Dr.		20,000	
	To 10% Debentures A/c				4,00,000
	(Issue of 4,000 Debentures of ₹100 each at 5% discount calculated as follows : $\frac{3,80,000}{95} = 4,000$ Debentures)				
April 1	Bank A/c	Dr.		45,000	
	To Bank Loan A/c				45,000
	(Loan taken from bank)				
April 1	Debentures Suspense A/c	Dr.		50,000	
	To 11% Debentures A/c				50,000
	(Issue of 500, 11% debentures of ₹100 each as collateral security to secure a loan of 45,000 from the Bank)				
April 1	Bank A/c	Dr.		5,00,000	
	To 12% Debentures Application & Allotment A/c				5,00,000
	(Application money received for 5,000 debentures @₹100 each)				

April 1	Debenture Application & Allotment A/c ... Dr.		5,00,000	
	Loss on Issue of Debentures A/c ... Dr.		25,000	
	To 12% Debentures A/c			5,00,000
	To Premium on Redemption of Debentures A/c			25,000
	(Debentures issued at par, redeemable at a premium of 5%)			
Sept. 30	Interest on Debentures A/c ... Dr.		50,000	
	To Debentureholders A/c			40,000
	To TDS A/c			10,000
	(Half-yearly interest due on debentures and tax deducted at source)			
Sept. 30	Debentureholders A/c ... Dr.		40,000	
	To Bank A/c			40,000
	(Payment of interest)			
Sept. 30	TDS A/c ... Dr.		10,000	
	To Bank A/c			10,000
	(TDS deposited in Government Account)			
2014 March 31	Interest on Debentures A/c ... Dr.		50,000	
	To Debentureholders A/c			40,000
	To TDS A/c			10,000
	(Half-yearly interest due on debentures and tax deducted at source)			
March 31	Debentureholders A/c ... Dr.		40,000	
	To Bank A/c			40,000
	(Payment of interest)			
March 31	TDS A/c ... Dr.		10,000	
	To Bank A/c			10,000
	(TDS deposited in Government Account)			
March 31	Statement of Profit & Loss ... Dr.		1,00,000	
	To Interest on Debentures A/c (₹50,000 + ₹50,000)			1,00,000
	(Interest transferred to Statement of Profit and Loss)			
March 31	Security Premium Reserve A/c ... Dr.		45,000	
	To Loss on Issue of Debentures			25,000
	To Discount on Issue of Debentures A/c			20,000
	(Loss and discount on issue of debentures written off)			

Working Note :

(1) Interest on Debentures for half year :

$$4,00,000 \times \frac{10}{100} \times \frac{6}{12} = 20,000$$

$$5,00,000 \times \frac{12}{100} \times \frac{6}{12} = 30,000$$

$$\underline{\underline{50,000}}$$

(2) Interest is not paid on debentures issued as collateral security.

ILLUSTRATION 31.

On 1st April, 2013, Sunshine Ltd. issued ₹10,00,000, 15% Debentures of ₹100 each at 8% discount payable :

₹40 on application

The balance on allotment.

These debentures were to be redeemed at a premium of 5% after five years. All the debentures were subscribed for by the public.

Interest on these debentures was to be paid half-yearly which was duly paid by the company.

You are required to :

(*i*) Pass journal entries in the first year of debenture issue (including entries for debenture interest.) Company decided to write off entire Loss on Issue of Debentures in the first year itself.

(*ii*) Prepare the 15% Debenture Account for the year ending 31st March, 2014.

(ISC, 2015)

SOLUTION :

Books of Sunshine Ltd.

JOURNAL

Date	*Particulars*		*L.F.*	*Dr.*	*Cr.*
2013				₹	₹
April 1	Bank A/c	Dr.		4,00,000	
	To 15% Debenture Application A/c				4,00,000
	(Receipt of application money on 10,000 debentures @ ₹40 each)				
April 1	15% Debenture Application A/c	Dr.		4,00,000	
	To 15% Debentures A/c				4,00,000
	(Application money transferred to Debentures Account)				
April 1	15% Debenture Allotment A/c	Dr.		5,20,000	
	Loss on issue of Debentures A/c	Dr.		1,30,000	
	To 15% Debentures A/c				6,00,000
	To Premium on Redemption of Debentures A/c				50,000
	(Amount due @ ₹52 each on 10,000 debentures issued at 8% discount and redeemable at 5% premium)				
April 1	Bank A/c	Dr.		5,20,000	
	To 15% Debenture Allotment A/c				5,20,000
	(Allotment money received)				
Sept. 30	Interest on Debentures A/c	Dr.		75,000	
	To Debenture holders A/c				75,000
	(Interest on Debentures due for half year)				

Sept. 30	Debenture holders A/c	Dr.	75,000	
	To Bank A/c			75,000
	(Interest on Debentures paid)			
2014 March 31	Interest on Debentures A/c	Dr.	75,000	
	To Debenture holders A/c			75,000
	(Interest on Debentures due for half year)			
March 31	Debenture holders A/c	Dr.	75,000	
	To Bank A/c			75,000
	(Interest on Debentures paid)			
March 31	Statement of Profit and Loss	Dr.	2,80,000	
	To Interest on Debentures A/c			1,50,000
	To Loss on Issue of Debentures A/c			1,30,000
	(Interest on Debentures and Loss on Issue Written Off from Statement of P & L)			

Dr. 15% DEBENTURES ACCOUNT Cr.

Date	Particulars	J.F.	₹	Date	Particulars	J.F.	₹
2014 March 31	To Balance c/d		10,00,000	2013 April 1	By 15% Debenture Application A/c		4,00,000
				April 1	By 15% Debenture Allotment A/c		5,20,000
				April 1	By Loss on Issue of Debentures A/c		80,000
			10,00,000				10,00,000

ILLUSTRATION 32.

During the year 2014-15, Anderson Ltd. issued 12% Debentures of ₹100 each, as per the details given below :

(*a*) 900 Debentures issued as collateral security to a bank against a loan of ₹60,000.

(*b*) The underwriters were to be paid a commission of ₹48,000. 25% of the amount was paid to them in cash and balance was paid by the issue of Debentures at a discount of 10%, to be redeemed at par.

(*c*) A machine was purchased for ₹2,18,500. The vendor was paid by the issue of Debentures at a premium of 15%, to be redeemed at par.

(*d*) 5,000 Debentures were issued to the public at 5% premium, to be redeemed at a premium of 5%.

The company wrote off all capital losses arising from the issue of Debentures at the end of the year from its capital profits and if need be from its revenue profits.

You are required to journalise the above transactions in the books of Anderson Ltd. *(ISC 2016)*

SOLUTION :

Anderson Ltd.

JOURNAL

Date	*Particulars*		*L.F.*	*Dr.*	*Cr.*
				₹	₹
(*a*)	Bank A/c	Dr.		60,000	
	To Bank Loan A/c				60,000
	(Loan taken from the bank)				
	Debenture Suspense A/c	Dr.		90,000	
	To 12% Debentures A/c				90,000
	(900 Debentures of ₹100 each issued as a collateral security for bank loan)				
(*b*)	Underwriting Commission A/c	Dr.		48,000	
	To Underwriters				48,000
	(Commission due to underwriters)				
	Underwriters	Dr.		12,000	
	To Cash A/c				12,000
	(Cash paid to underwriters)				
	Underwriters	Dr.		36,000	
	Discount on Issue of Debentures A/c	Dr.		4,000	
	To 12% Debentures A/c				40,000
	(400 Debentures of ₹100 each issued to Underwriters)				
(*c*)	Plant and Machinery A/c	Dr.		2,18,500	
	To Vendor				2,18,500
	(Plant & Machinery purchased)				
	Vendor	Dr.		2,18,500	
	To 12% Debentures A/c				1,90,000
	To Securities Premium Reserve A/c				28,500
	(1,900 Debentures of ₹100 each issued to vendor)				
(*d*)	Bank A/c	Dr.		5,25,000	
	To Debenture Application & Allotment A/c				5,25,000
	(Application and Allotment amount received)				
	Debenture Application & Allotment A/c	Dr.		5,25,000	
	Loss on Issue of Debentures A/c	Dr.		25,000	
	To 12% Debentures A/c				5,00,000
	To Securities Premium Reserve A/c				25,000
	To Premium on Redemption of Debentures A/c				25,000
	(5,000 Debentures issued to the public)				

	Security Premium Reserve A/c Dr.		53,500	
	Statement of Profit & Loss Dr.		23,500	
	To Underwriting Commission A/c			48,000
	To Discount on Issue of Debentures A/c			4,000
	To Loss on Issue of Debentures A/c			25,000
	(Capital losses written off)			

ILLUSTRATION 33.

On 1st April, 2015 Max Ltd. took over assets of ₹4,50,000 and liabilities of ₹60,000 of Prudence Ltd. for the purchase consideration of ₹4,40,000. It paid the purchase consideration by issuing 8% Debentures of ₹100 each at 10% premium. On the same date it issued another 3,000 8% Debentures of ₹100 each at a discount of 10%, redeemable at a premium of 5% after 5 years. According to the terms of the issue ₹30 is payable on application and the balance on the allotment of debentures.

You are required to pass journal entries in the books of Max Ltd. to record the above transactions. Entire loss on issue of debentures is to be written off in the first year itself. *(ISC Sample Paper, 2017)*

SOLUTION :

JOURNAL OF MAX LTD.

Date	*Particulars*	*L.F.*	*Dr.*	*Cr.*
			₹	₹
2015				
April 1	Sundry Assets A/c Dr.		4,50,000	
	Goodwill A/c (Balancing Figure) Dr.		50,000	
	To Sundry Liabilities A/c			60,000
	To Prudence Ltd.			4,40,000
	(Purchase of assets and liabilities of Prudence Ltd.)			
April 1	Prudence Ltd. Dr.		4,40,000	
	To 8% Debentures A/c			4,00,000
	To Securities Premium Reserve A/c			40,000
	(Issue of 4,000 Debentures of ₹100 each at 10% premium, calculated as follows : $\frac{4,40,000}{110} = 4,000$ Debentures)			
April 1	Bank A/c Dr.		90,000	
	To 8% Debenture Application A/c			90,000
	(Receipt of application money on 3,000 debentures @ ₹30 each)			
April 1	8% Debenture Application A/c Dr.		90,000	
	To 8% Debentures A/c			90,000
	(Application money transferred to Debentures Account)			
April 1	8% Debenture Allotment A/c Dr.		1,80,000	
	Loss on issue of Debentures A/c Dr.		45,000	
	To 8% Debentures A/c			2,10,000
	To Premium on Redemption of Debentures A/c			15,000
	(Amount due @ ₹60 each on 3,000 debentures issued at 10% discount and redeemable at 5% premium)			

April 1	Bank A/c	Dr.		1,80,000	
	To 8% Debenture Allotment A/c				1,80,000
	(Allotment money received)				
April 1	Securities Premium Reserve A/c	Dr.		40,000	
	Statement of Profit & Loss A/c	Dr.		5,000	
	To Loss on Issue of Debentures A/c				45,000
	(Loss on issue written off)				

SHORT ANSWER QUESTIONS

(Questions Carrying 2 Marks)

1. What is a debenture? What are the types of debentures?
2. What is meant by 'Mortgage Debenture'?
3. What is meant by 'Bearer Debenture'?
4. What is 'Registered Debenture'?
5. What is meant by 'Redeemable Debenture'?
6. What is meant by 'Irredeemable Debenture'? *(I.S.C. 2002)*
7. What is the difference between redeemable and irredeemable debenture?
8. What is convertible debenture?
9. State the meaning of Fully Convertible and Partly Convertible Debentures.

Ans. **Fully Convertible Debentures (FCD)** are those debenutres where the full amount of debentures is convertible into shares.

Partly Convertible Debentures (PCD) are those debentures where only a part of the amount of debentures is convertible into shares.

10. Write any three points of differences between an equity share and a debenture.
11. What is the nature of debenture interest? *(C.B.S.E. 2020)*

Ans. Interest on debentures is a charge against the profits of the company and is payable whether the company makes a profit or loss.

12. What is meant by 'debentures issued at par but redeemable at premium'?
13. What is meant by 'debentures issued at discount and redeemable at premium'?
14. What is Zero Coupon Bond?

Ans. A Zero Coupon Bond is one which does not carry any specific rate of interest. In order to compensate the investors, such bonds are issued at a substantial discount. The difference between issue price and the redemption price represents the total interest to be spread over the duration of the bond. A proportionate amount of total interest is charged to Statement of Profit and Loss every year over the lifetime of bond.

15. Mention two differences between 'Premium on Issue of Debentures' and 'Premium on Redemption of Debentures. *(ISC Sample Paper, 2017)*

Ans. Distinction between 'Premium on Issue' and 'Premium on Redemption' of Debentures :

Premium on Issue of Debentures	*Premium on Redemption of Debentures*
1. It is a capital profit and is used in writing off capital losses.	It is a capital loss.
2. It is shown on the liabilities side under the head 'Reserves and Surplus'.	It is a liability and appears under the head "Non Current Liabilities" under sub-head Long term Borrowings till the redemption of debentures.

16. Why is premium on the issue of debentures considered a capital profit? *(I.S.C. 2007, 2014)*

Ans. It is considered as a capital profit because it is not an income arising from the normal course of business operations.

17. Interest on debentures has to be paid even if the company is not earning a profit. Justify. *(I.S.C. 2007)*

Ans. Interest payable on debentures constitutes a charge against profits and is to be paid even if the company is not earning a profit. It is justified because debenture is an acknowledgement of a debt. Debentureholders are not the owners of the company and will not get higher interest in the periods when the company will be earning huge profits.

18. State two differences between Share Capital and Loan Capital. *(I.S.C. 2009)*

Ans. (*i*) Providers of share capital i.e. shareholders are the owners of the company whereas providers of loan capital e.g. debentureholders are the creditors of the company.

(*ii*) Shareholders get dividend from the company whereas debentureholders get interest from the company.

19. What is meant by issue of debentures as purchase consideration?

Ans. When a company issues debentures for purchase of an asset like land and building, machinery etc. it is called 'Issue of Debentures as Purchase Consideration.'

20. When does Loss on Issue of Debentures arise? *(I.S.C. 2013)*

Ans. Loss on Issue of Debentures arises at the time of Issue of Debentures when they are redeemable at premium.

21. What is the nature of loss on Issue of Debentures?

Ans. It is a loss of capital nature.

22. What is the accounting treatment of 'Loss on Issue of Debentures'?

Ans. As per ISC Council's instructions Discount or Loss on Issue of Debentures are to be written off from Securities Premium Reserve (if it exists) or from General Reserve or Surplus *i.e.*, Balance in Statement of Profit and Loss under the head 'Reserves and Surplus' in the year in which they occur or proportionately each year when debentures are redeemable in instalments.

23. What is meant by "issue of debentures as collateral security"? *(I.S.C. 2010)*

24. What is the accounting treatment when debentures are issued as a collateral security? *(I.S.C. 2014)*

Ans. Debentures issued as a collateral security can be dealt with in two ways in the books :

(*i*) **First Method** : In this method no entry is recorded in the books of accounts. However, the fact that the debentures have been issued as collateral security is disclosed under the head 'Secured Loans' on the Equity & Liabilities side of the Balance Sheet.

(*ii*) **Second Method** : Following entry is passed in this method :

Debenture Suspense A/c	Dr.	(This appears on the Assets side)
To Debentures A/c		(This appears on the Equity & Liabilities Side)
(Issue of debentures as collateral security)		

25. Give the adjusting entry and closing entry for interest on debentures due to the debenture holders of a company. *(ISC 2016)*

Ans. Adjusting entry :

Interest on Debentures A/c Dr.
To Debentureholders A/c

Closing entry :

Statement of Profit & Loss Dr.
To Interest on Debentures A/c

26. 'A Company has to pay interest on debentures prior to paying dividend on shares'. Justify. *(ISC Sample Paper, 2017)*

Ans. Debenture interest is the cost of using the amount borrowed by a Company. It is a deductible expense for computing the net profit of a Company. Hence, it is an expense shown under finance costs in the statement of profit and loss of a Company. In other words, it is a charge against profits of the Company and is payable whether profits are earned or not. On the other hand, dividend is an appropriation of profits. A Company can pay dividend only when it earns profits. Hence, it is justified to pay interest prior to paying dividend.

PRACTICAL QUESTIONS

(Question No. 1 to 29 are strictly in the serial order of Illustrations)

Issue of Debentures at Par

Q. 1. Y Ltd. issued 2,000, 15% debentures of ₹100 each at Par, payable as follows: ₹25 on Application; ₹25 on Allotment and ₹50 on First and Final Call.

Applications were received for 3,000 debentures. Applications for 1,600 debentures were accepted in full. Applications for 600 debentures were allotted 400 debentures and the rest were rejected. All moneys due were received except final call on 100 debentures.

Pass necessary journal entries.

[**Ans.** Cash at Bank ₹1,95,000.]

At Premium

Q. 2. *X* Ltd. issued 5,000, 12% Debentures of ₹100 each at a premium of ₹5 payable as follows :

On Application	₹30 (including premium)
On Allotment	₹40
On Ist and Final Call	The balance amount

Applications were received for 6,000 debentures and allotment was made pro-rata to all applicants. All the moneys were duly received. Pass necessary journal entries.

[**Ans.** Cash at Bank ₹5,25,000. Cash received on allotment ₹1,70,000 and on first call ₹1,75,000.]

At Discount

Q. 3. *R* Ltd. issued 8,000, 13% Debentures of ₹100 each at a discount of 5% payable as follows :

On Application	₹25
On Allotment	₹25
On First and Final Call	The balance amount

Public applied for 6,000 debentures. All the moneys were duly received. Expenses on issue of debentures amounted to ₹20,000.

Pass journal entries and show the above accounts in the Company's Balance Sheet at the end of the first year. Company decided to write off the discount on issue of debentures in the first year itself.

[**Ans.** Cash at Bank ₹5,50,000.]

Consideration other than Cash

Q. 4. *X* Company purchased assets of the book value of ₹10,45,000 from *Y* Co. It was agreed that the purchase consideration be paid by issuing 14% Debentures of ₹100 each. Assume debentures have been issued (*i*) at par; (*ii*) at a discount of 5%, and (*iii*) at a premium of 10%.

Give necessary journal entries in the books of *X* Company. Discount on issue of debentures is to be written off in the first year itself.

[**Ans.** Number of Debentures issued in Case (I) 10,450; Case (II) 11,000, and Case (III) 9,500.]

Q. 5. Golden Ltd. bought assets for ₹5,50,00,000 and assumed liabilities worth ₹1,26,00,000 from Silver Ltd. and issued 8% Debentures of ₹500 each at a premium of 6%. Record necessary entries in the books of Golden Ltd.

[**Ans.** Number of Debentures Issued 80,000.]

Q. 6. Disha Ltd. took over assets of ₹8,00,000 and liabilities of ₹3,00,000 from Kirti Ltd. for a purchase consideration of ₹6,00,000. The payment was made by issue of 9% Debentures of ₹100 each at 20% premium.

Pass the necessary journal entries for the above transactions in the books of Disha Ltd.

(C.B.S.E. 2020, Punjab)

[**Ans.** Goodwill ₹1,00,000; Debentures issued : 5,000 Debentures of ₹100 each.]

Q. 7. A Company purchased Assets of the book value of ₹12,00,000 and Liabilities of ₹2,20,000 of another Company for a purchase consideration of ₹9,40,000. The purchase consideration was discharged by the issue of debentures of ₹500 each at a discount of 6%. Pass journal entries in the books of purchasing company. It is the policy of the Company to write off all capital losses in the first year itself.

[**Ans.** Capital Reserve ₹40,000; Debentures issued : 2,000 Debentures of ₹500 each.]

Q. 8. Moon Craft Ltd. purchased machinery for ₹2,70,000. As per the agreement, the payment is to be made by issuing sufficient number of 5% Debentures of ₹100 each.

You are required to calculate number of debentures to be issued & pass the necessary journal entries in the books of the Company if the said Debentures are issued:

(*i*) at a discount of 10%.

(*ii*) at a premium of 20%. *(I.S.C. Specimen Question Paper, 2018)*

Discount on issue is to be written off in the very first year.

[**Ans.** No. of Debentures issued : Case (*i*) 3,000; Case (*ii*) 2,250.]

Q. 9. *J* Ltd. purchased machinery for ₹3,50,000 from *K* Ltd. on 28.2.2018. ₹50,000 were paid to *K* Ltd. immediately and the balance was paid by issue of 10% debentures of ₹3,10,000 in *J* Ltd. Pass the necessary journal entries including writing off discount on issue of debentures.

[**Ans.** Discount on issue of debentures will be debited by ₹10,000.]

Q. 10. *X* Ltd. purchased assets of ₹8,00,000 and liabilities of ₹1,00,000 from *Y* Ltd. on 1.4.2022. ₹2,00,000 were paid immediately and the balance was paid by issue of ₹4,75,000, 10% debentures in *X* Ltd. Give journal entries in the books of *X* Ltd.

[**Ans.** Securities Premium Reserve will be credited by ₹25,000.]

Q. 11. Star Textiles Ltd. purchased assets of Modern Textiles Ltd. as under :

Land and Buildings of ₹25,00,000 at ₹40,00,000; Plant and Machinery of ₹10,00,000 for ₹7,50,000 and Furniture of ₹3,00,000 for ₹1,00,000 for purchase consideration of ₹45,00,000. Star Textiles Ltd. paid ₹3,00,000 in cash and remaining by issue of 9% Debentures of ₹500 each at a premium of 5%. Record necessary entries in the books of Star Textiles Ltd.

[**Ans.** Capital Reserve ₹3,50,000; Debentures issued : 8,000 Debentures of ₹500 each.]

Q. 12. Gunjan Limited purchased a running business from Vrindavan Limited for a sum of ₹25,00,000, payable ₹4,00,000 by cheque and for the balance issued 8% Debentures of ₹100 each at 5% premium.

The assets and liabilities consisted of the following :

	Book Value (₹)	*Agreed Value* (₹)
Land and Buildings	5,00,000	9,00,000
Plant and Machinery	10,00,000	8,00,000
Patents	1,00,000	40,000

Sundry Debtors	8,00,000	Subject to 5% Provision
Stock	6,00,000	4,40,000
Sundry Creditors	1,20,000	1,20,000

Record necessary journal entries in the books of Gunjan Limited.

[**Ans.** Capital Reserve ₹3,20,000; Number of Debentures issued 20,000]

Issue of Debentures as Collateral Security

Q. 13. *X* Ltd. had ₹25,00,000, 11% Debentures outstanding as on 1st April, 2021. During the year it took a loan of ₹5,00,000 from Punjab National Bank for which the Company placed with the bank debentures for ₹6,00,000 as Collateral Security. Pass journal entries, if any. Also show how the Debentures and Bank Loan will appear in the Company's Balance Sheet as at 31st March, 2022.

Q. 14. Hassan Limited took a loan of ₹30,00,000 from a bank against primary security worth ₹40,00,000 and issued 35,000, 6% debentures of ₹100 each as a collateral security. The company again after one year took a loan of ₹50,00,000 from bank against Plant as primary security and deposited 60,000, 6% debentures of ₹100 each as collateral security. Record necessary journal entries. How will you show the issue of debentures and bank loan in the balance sheet of the company.

Q. 15. India Ltd. made the following issue of 6% debentures :

(*i*) For cash at 90%, 6,000 debentures of ₹100 each.

(*ii*) 1,100 debentures of ₹100 each to a creditor regarding machinery costing ₹1,00,000.

(*iii*) To bank for a loan of ₹7,00,000 as collateral security 10,000 debentures of ₹100 each.

Prepare necessary entries ignoring writing off discount on issue of debentures.

[**Ans.** (*i*) Discount on Issue of Debentures ₹60,000;
(*ii*) Discount on Issue of Debentures ₹10,000;
(*iii*) Dr. Bank A/c; Cr. Bank Loan A/c by ₹7,00,000, and
Dr. Debenture Suspense A/c; Cr. Debentures A/c by ₹10,00,000.]

Q. 16. *X* Ltd. issued 25,000, 9% Debentures of ₹100 each at a premium of ₹4 per debenture on 1st April, 2021. On the same date it purchased assets of ₹10,00,000 and took over liabilities of ₹70,000 of *Y* Ltd. and paid ₹4,00,000 in Cash and remaining by issue of ₹5,00,000, 9% debentures at a premium of 6%. On the same date it took a loan from the Bank for ₹6,00,000 and issued 9% debentures as collateral security. Give entries and the extract of Balance Sheet on 31st March, 2022. Ignore interest.

[**Ans.** Securities Premium Reserve ₹1,30,000.]

Accounting for Issue of Debentures Considering the Terms and Conditions of Redemption

Q. 17. What journal entries will be made in the following cases :

(*i*) A company issued ₹40,000, 12% Debentures at par, redeemable also at par.

(*ii*) A company issued ₹40,000, 12% Debentures at a discount of 10% redeemable at par;

(*iii*) A company issued ₹40,000, 12% Debentures at a premium of 5% redeemable at par;

(*iv*) A company issued ₹40,000, 12% Debentures at par, redeemable at 10% premium; and

(*v*) A company issued ₹40,000, 12% Debentures at a discount of 5% and redeemable at 5% premium.

Note. The face value of a 12% Debenture is ₹100. Assume that the discount or loss on issue of debentures is to be written off in the first year itself.

Q. 18. Journalise the transactions given below :

(*i*) A debenture issued at ₹ 95, repayable at ₹100.

(*ii*) A debenture issued at ₹ 95, repayable at ₹105.

(*iii*) A debenture issued at ₹100, repayable at ₹105.

(*iv*) A debenture issued at ₹105, repayable at ₹100.

The face value of debenture in each of the above case is ₹100.

Interest on Debentures

Q. 19. On 1-4-2015, K.K. Ltd. issued 500, 9% Debentures of ₹500 each at a discount of 4%, redeemable at a premium of 5% after three years.

Pass necessary Journal Entries for the issue of debentures and debenture interest for the year ended 31-3-2016 assuming that interest is payable on 30th September and 31st March and the rate of tax deducted at source is 10%. The company closes its books on 31st March every year. Ignore writing off loss on issue.

(C.B.S.E. 2017, Delhi)

[**Ans.** Total Interest of ₹22,500 will be transferred to Statement of Profit & Loss on 31st March, 2016.]

Writing off Discount on Issue of Debentures

Q. 20. On 1st April, 2022, Luxury Cosmetics Ltd. issued 30,000, 9% debentures of ₹500 each at a discount of 4%, redeemable at a premium of 5% after 4 years payable as : ₹200 on application and balance on allotment. Record necessary entries for issue of debentures. Luxury cosmetics has a balance of ₹20,00,000 in Securities Premium Reserve. Entire loss on issue is to be written off in the first year itself.

[**Ans.** Loss on Issue will be written off against Securities Premium Reserve.]

Q. 21. *X* Ltd. issued on 1st April, 2021, 50,000, 7% Debentures of ₹100 each at 4% discount redeemable after five years at a premium of ₹10. All the debentures were subscribed. During the year ended 31st March, 2019, the company earned a profit of ₹1,20,000. It has balance of ₹5,50,000 in Securities Premium Reserve.

Pass the Journal entries and prepare an extract of Balance Sheet as at 31st March, 2022 showing Loss on Issue of Debentures which is to be written off in the first year itself.

[**Ans.** Loss shown under the Head 'Reserves and Surplus' ₹30,000.]

Q. 22. *X* Ltd. issued 5,000, 8% Debentures of ₹200 each at a premium of 6% redeemable at a premium of 5% after 5 years. According to the terms of issue, ₹80 was payable on application and balance on allotment.

Record necessary Journal entries at the time of issue of Debentures assuming that the entire loss on issue is to be written off in first year.

[**Ans.** Loss on issue ₹50,000 will be written off against securities premium reserve]

Q. 23. On 1st April, 2018 a Limited Co. issued 7,000 debentures of ₹200 each at a discount of 5%. Debentures were to be redeemed at the end of seven years at par. Pass journal entries for the issue and show the 'Discount on Issue of Debentures A/c' for 4 years. Accounts are closed on 31st March each year.

[**Ans.** Discount to be written off each year ₹10,000.]

Q. 24. On 1st April, 2018, a Limited Company issued debentures of the face value of ₹5,00,000 at a discount of 6%. The debentures were repayable in 5 years by annual drawings of ₹1,00,000 made on 31st March each year.

Calculate the amount of discount to be written off each year and show the Discount on Issue of Debentures A/c for the first three years.

[**Ans.** Discount to be written off I year ₹10,000; II year ₹8,000; III year ₹6,000; IV year ₹4,000; V year ₹2,000; Balance of Discount on Issue of Debentures A/c at the end of 3rd year ₹6,000.]

Q. 25. On 1st April, 2015 a Limited Company issued 10% Debentures of the face value of ₹1,20,000 at a discount of 6%. The debentures are repayable by annual drawings of ₹40,000 commencing from the end of 3rd year. How will you deal with discount on debentures?

Show the discount on issue of debentures account in the Company's ledger for the period of duration of debentures. Assume that the accounts are closed on 31st March each year.

[**Ans.** Discount to be written off :— 1st year ₹1,800; 2nd year ₹1,800; 3rd year ₹1,800; 4th year ₹1,200; 5th year ₹600.]

Q. 26. On 1st April, 2015, *X* Ltd. issued 5,000, 8% debentures of ₹200 each at a discount of 5% repayable as follows :—

On 31st March, 2018	₹3,00,000
On 31st March, 2019	₹4,00,000
On 31st March, 2020	₹3,00,000

Prepare 'Discount on Issue of Debentures A/c' for five years.

[**Ans.** 1st year ₹12,500; 2nd year ₹12,500; 3rd year ₹12,500; 4th year ₹ 8,750; 5th year ₹3,750.]

Q. 27. *P* Ltd. issued 6,000 12% Debentures of ₹100 each at a discount of 6% to be redeemed as follows :

1st year : Nil; 2nd year : Nil; 3rd year : ₹4,00,000; 4th year : ₹2,00,000. Show the Discount on Issue of Debentures Account for the period of 4 years in the books of the Company.

[**Ans.** Discount to be written off 1st year ₹10,800; 2nd year ₹10,800; 3rd year ₹10,800 and 4th year ₹3,600.]

Q. 28. Supriya Ltd. issued 80 Lakh 9% debentures of ₹100 each at a discount of 6% on April 1, 2012. Debentures are repayable in five equal instalments starting from the end of sixth year. The securities premium account showed a balance of ₹1.6 crores on the above date. Compute the amount of discount to be written off and pass journal entries to record these transactions in the books of Supriya Ltd.

[**Ans.** Discount to be written off : From March 31, 2013 to March 31, 2018 = ₹0.4 Crore each year; On March 31, 2019 ₹0.32 Crore; On March 31, 2020 ₹0.24 Crore; On March 31, 2021 ₹0.16 Crore; On March 31, 2022 ₹0.08 Crore.]

Q. 29. Malhotra Jewellery Ltd. issued 30 Lakh, 9% Debentures of ₹200 each at ₹194 on April 1, 2015 redeemable at premium of 5% as follows :

12 Lakh Debentures on March 31, 2020
6 Lakh Debentures on March 31, 2021
Balance Debentures on March 31, 2022

Compute the amount of discount/loss on issue of debentures to be written off each year and also prepare the loss on issue of debentures account.

[**Ans.** Loss on issue of debentures to be written off : From March 31, 2016 to March 31, 2020 ₹0.8 Crore each year; On March 31, 2021 ₹0.48 Crore and on March 31, 2022 ₹0.32 Crore.]

ADDITIONAL QUESTIONS

Q. 30. Suvidha Ltd. purchased machinery for ₹1,98,000 from Suppliers Ltd. The payment was made by issue of 12% debentures of ₹100 each. Pass necessary journal entries for the purchase of machinery and issue of debentures when

(*i*) Debentures are issued at par.
(*ii*) Debentures are issued at 10% discount.
(*iii*) Debentures are issued at 10% premium.

Ignore writing off discount on issue.

[**Ans.** Number of Debentures issued in Case (*i*) 1,980; Case (*ii*) 2,200 and Case (*iii*) 1,800.]

Q. 31. Deepak Ltd. purchased furniture of ₹2,20,000 from M/s Furniture Mart. 50% of the amount was paid to Furniture Mart by accepting a bill of exchange and for the balance the company issued 9% debentures of ₹100 each at a premium of 10% in favour of Furniture Mart.

Pass necessary journal entries in the books of Deepak Ltd. for the above transactions.

[**Ans.** Debentures issued of the face value of ₹1,00,000. Securities Premium Reserve ₹10,000.]

Q. 32. Vayee Ltd. purchased the following assets of E.X. Ltd. :

Land and Building of ₹60,00,000 at ₹84,00,000; Plant and Machinery of ₹40,00,000 at ₹36,00,000.

The purchase consideration was ₹1,10,00,000. Payment was made by accepting a Bill of Exchange in favour of E.X. Ltd. of ₹20,00,000 and remaining by issue of 8% debentures of ₹100 each at a premium of 20%.

Record the necessary journal entries for the above transactions in the books of Vayee Ltd. *(C.B.S.E. 2020, Mumbai, Chennai)*

[**Ans.** Capital Reserve ₹10,00,000; Number of Debentures issued 75,000]

Q. 33. Tushar Ltd. purchased assets of ₹14,40,000 and liabilities of ₹2,55,000 from Chander Ltd. on 1.4.2022. ₹2,40,000 were paid immediately. Pass journal entries in the books of Tushar Ltd. if the balance was paid as follows :

Case (*i*) by issue of ₹ 9,00,000, 11% debentures in Tushar Ltd.

Case (*ii*) by issue of ₹10,50,000, 12% debentures in Tushar Ltd.

[**Ans.** Case (*i*) Securities Premium Reserve will be credited by ₹45,000; Case (*ii*) Discount on issue of debentures will be debited by ₹1,05,000.]

Q. 34. A Company purchased assets of the book value of ₹6,00,000 and took over liabilities of ₹1,50,000 from Golden Ltd. It was agreed that the purchase consideration settled at ₹4,80,000 be paid by issuing debentures of ₹100 each at a premium of 10%. It was further agreed that any fraction of the debenture be paid in cash. Give journal entries in the books of purchasing company.

SOLUTION : JOURNAL

Date	*Particulars*		*L.F*	*Dr.*	*Cr.*
				₹	₹
	Sundry Assets A/c	Dr.		6,00,000	
	Goodwill A/c (Balancing Figure)	Dr.		30,000	
	To Sundry Liabilities A/c				1,50,000
	To Golden Ltd.				4,80,000
	(Purchase of assets and liabilities of the Vendor company)				
	Golden Ltd.	Dr.		4,80,000	
	To Debentures A/c				4,36,300
	To Securities Premium Reserve A/c				43,630
	To Bank A/c				70
	(Issue of 4,363 debentures of ₹100 each at 10% premium and the balance paid in cash)				

Working Note : Number of Debentures to be issued $= \frac{4,80,000}{110} = 4363.63$ or 4,363

Q. 35. *X* Ltd. took over assets of ₹5,00,000 and liabilities of ₹1,00,000 of another company at an agreed price of ₹3,80,000. The purchase consideration was discharged by issuing debentures of ₹100 each at a discount of 10%. It was agreed that any fraction of the debenture be paid in cash. Give journal entries in the books of *X* Ltd.

SOLUTION : JOURNAL

Date	*Particulars*		*L.F.*	*Dr*	*Cr.*
				₹	₹
	Sundry Assets A/c	Dr.		5,00,000	
	To Sundry Liabilities A/c				1,00,000
	To Capital Reserve A/c (Balancing Figure)				20,000

	To Vendor Co. (Purchase of assets and liabilities of the Vendor Company)			3,80,000
	Vendor Co. Dr.		3,80,000	
	Discount on Issue of Debentures A/c Dr.		42,220	
	To Debentures A/c			4,22,200
	To Bank A/c			20
	(Issue of 4,222 debentures of ₹100 each at 10% discount and the balance paid in cash)			

Working Note : Number of Debentures to be issued $= \frac{3,80,000}{90} = 4,222.22$ or 4,222

Q. 36. Oberoi Ltd. took certain fixed assets for ₹6,30,000 from Vikram Ltd. and allotted 6,000, 12% Debentures at a premium of 5% to satisfy the purchase consideration. The Company then issued a prospectus inviting the public to subscribe to 20,000, 11% Debentures of ₹100 each at a discount of 2%, payable as ₹35 on application, ₹23 on allotment and the balance on first and final call.

Applications were received for 16,000 debentures only. All the applications were accepted and money received except first and final call on 100 debentures. Prepare the Cash Book and the Journal.

[**Ans.** Cash at Bank ₹15,64,000. Amount received on allotment ₹3,68,000 and on First Call ₹6,36,000.]

Q. 37. *X* Ltd. raised a bank loan of ₹10,00,000 and issued by way of collateral security 10,000, 12% Debentures of ₹100 each. The Company further issued to public 15,000, 12% Debentures of ₹100 each at 2% discount payable ₹30 on application, ₹18 on allotment, ₹20 on first call and the balance a month later. The public applied for 20,000 debentures. Applications for 12,000 debentures were accepted in full, applications for 4,000 debentures were allotted 3,000 debentures and the remaining applications were rejected. All amounts were duly received. Prepare journal entries and show the Balance Sheet. Discount on issue of debentures is to be written off in the first year itself.

[**Ans.** BALANCE SHEET

Particulars	*Note No.*	*Current Year* ₹	*Previous Year* ₹
I. EQUITY AND LIABILITIES			
Shareholder's Funds :			
Reserve and Surplus	1	(30,000)	
Non-Current Liabilities :			
Long-term Borrowings	2	25,00,000	
II. ASSETS			
Current Assets :			
Cash and Bank Balance	3	24,70,000	

Notes to Accounts :

	₹	₹
(1) **Reserve and Surplus :**	(30,000)	
Statement of Profit & Loss Balance (Discount on Issue of Debentures)		
(2) **Long-term Borrowings :**		
25,000, 12% Debentures of ₹100 each	25,00,000	
Less : Debenture Suspense A/c	10,00,000	
	15,00,000	
Bank Loan	10,00,000	
	25,00,000	
(3) **Cash & Bank Balance :**		
Cash at Bank	24,70,000	

Q. 38. Journalise the following transactions :

(*i*) 400 debentures issued at ₹ 960 each, repayable at ₹1,000 each.

(*ii*) 400 debentures issued at ₹1,040 each, repayable at ₹1,000 each.

(*iii*) 400 debentures issued at ₹1,000 each, repayable at ₹1,060 each.

(*iv*) 400 debentures issued at ₹960 each, repayable at ₹1,060 each.

(The face value of each debenture is ₹1,000)

Q. 39. Give the journal entries at the time of issue of debentures in the following cases :

(*i*) Issued ₹ 5,00,000, 12% debentures at par and redeemable at par after 5 years.

(*ii*) Issued ₹ 8,00,000, 11% debentures at 6% discount, redeemable at par after 4 years.

(*iii*) Issued ₹10,00,000, 14% debentures at 5% premium, redeemable at par after 4 years.

(*iv*) Issued ₹20,00,000, 12% debentures at par, redeemable at 5% premium after 3 years.

(*v*) Issued ₹12,00,000, 13% debentures at 4% discount, redeemable at 6% premium after 3 years.

Q. 40. A company issues the following debentures :

(*a*) 10,000, 12% debentures of ₹100 each at par but redeemable at a premium of 5% after 5 years;

(*b*) 10,000, 12% debentures of ₹100 each at a discount of 5%, but redeemable at a premium of 5% after 5 years;

(*c*) 5,000, 12% debentures of ₹100 each at a premium of 10% but redeemable at par after 5 years;

(*d*) 1,000, 14% debentures of ₹100 each issued to a supplier of machinery costing ₹95,000, the debentures are repayable after 5 years; and

(*e*) 300, 13% debentures of ₹100 each as a collateral security to a bank who has advanced a loan of ₹25,000 to the company for a period of 5 years.

Pass the Journal entries to record the issue of debentures.

Q. 41. Show by means of journal entries how would you record the following issues. Also show how they would appear in the respective Balance Sheets.

(*i*) *A* Ltd. issues ₹5,00,000, 13% Debentures at a discount of 8% redeemable at par.

(*ii*) *B* Ltd. issues ₹6,00,000, 12% Debentures at a discount of 6% redeemable at a premium of 7%.

(*iii*) *C* Ltd. purchased plant and machinery for ₹8,00,000 payable as to ₹2,30,000 in cash and the balance by an issue of 10% Debentures of ₹100 each at a discount of 5%.

(*iv*) *D* Ltd. issued 500, 11% Debentures of ₹100 each as a collateral security to a Bank who has advanced a loan of ₹45,000 to the Company for a period of 7 years.

(*v*) *E* Ltd. issued ₹2,20,000 Debentures to a creditor for ₹2,00,000 Capital Expenditure in satisfaction of his claim.

[**Ans.** In Case (*iii*) Number of Debentures issued 6,000;
In Case (*v*) Discount on Debentures ₹20,000.]

Q. 42. Maneesh Ltd. issued 10,000, 12% Debentures of ₹100 each at a discount of 6% to be redeemed as follows :

1st Year : Nil; 2nd Year : ₹5,00,000; 3rd Year : Nil; 4th Year : ₹5,00,000.

Show the Discount on Issue of Debentures Account for the period of 4 years.

[**Ans.** Discount to be written off 1st year ₹20,000; 2nd year ₹20,000; 3rd year ₹10,000 and 4th year ₹10,000.]

Q. 43. A Company issued 12% debentures of the face value of ₹17,60,000 at 97% on 1st April, 2016. The debentures are repayable by annual drawings of ₹4,40,000 commencing from the beginning of 5th year.

Show the 'Discount on Issue of Debentures A/c' for the period of duration of debentures. Assume that the accounts are closed on 31st March each year.

[**Ans.** Discount to be written off in the ratio of 4 : 4 : 4 : 4 : 3 : 2 : 1.]

Q. 44. A company issued 13% Debentures of ₹20,00,000 at 6% discount, redeemable at par. Assume further that debentures are to be redeemed by drawings method in the following manner :

Year-end	*Amount (Face Value)* ₹
3	8,00,000
5	6,00,000
7	6,00,000

Pass journal entries for issue of debentures and prepare Discount on Issue of Debentures Account for 7 years.

[**Ans.** Discount to be written off in the ratio of 20 : 20 : 20 : 12 : 12 : 6 : 6.]

Q. 45. *Y* Ltd. issued 12% Debentures of the face value of ₹6,00,000 at a discount of 5% repayable at par in equal proportion at the end of 5, 10 and 15 years.

Show the amount of discount to be written off at the end of each year.

[**Ans.** ₹3,000 every year for the first five years; ₹2,000 every year for the next five years; and ₹1,000 every year for the next five years.]

Q. 46. A Company issued 36,000, 11% Debentures of ₹50 each at a discount of 4%. The debentures are to be redeemed at par in equal proportions at the end of 4th, 8th and 12th years. Show the amount of discount to be written off at the end of each year.

[**Ans.** ₹9,000 every year for the first four years; ₹6,000 every year for the next four years and ₹3,000 every year for the next four years.]

Q. 47. *X* Ltd. issued 15,000, 10% Debentures of ₹200 each at a discount of 3%. The debentures are to be redeemed at the rate of ₹5,00,000 each year commencing with the end of 5th year. Calculate the amount of discount to be written off each year and show the discount on issue of debentures account for the first four years.

[**Ans.** Discount to be written off in the ratio of 30 : 30 : 30 : 30 : 30 : 25 : 20 : 15 : 10 : 5. Balance of Discount A/c at the end of 4th year ₹42,000.]

Q. 48. On April 1, 2013, *XY* Limited issued ₹9,00,000 10% debentures at a discount of 9%. The debentures were to be redeemed in three equal annual instalments starting from March 31, 2015. Prepare 'Discount on Issue of Debentures Account' for the first three years starting from April 1, 2013. Also show your workings clearly.

[**Ans.** Discount to be written off in the ratio of 3 : 3 : 2 : 1. Balance of Discount on Issue of Debentures A/c at the end of 3rd year ₹9,000.]

Q. 49. Boots Ltd. issued ₹6,00,000, 8% Debentures at a discount of 6%. The debentures were redeemable in four equal annual instalments. Pass necessary journal entries for issue of debentures and prepare 'Discount on issue of debentures Account' for four years. Show your workings clearly. *(C.B.S.E. 2018 Comptt.)*

[**Ans.** Discount to be written off in the ratio of 4 : 3 : 2 : 1]

Q. 50. Newtown Ltd. was formed on 1st April, 2012, with an authorized capital of ₹10,00,000 divided into equity shares of ₹10 each. It invited applications for 20,000 shares in the year of its formation, all of which were subscribed for and amount due on them fully received.

On 1st April, 2013, the company invited applications for another 50,000 shares. Applications for 45,000 shares were received. All calls were made and the amount received on them except the final call of ₹2 per share on 1,000 shares.

Out of the shares on which final call was not received, 600 were forfeited.

On 1st April, 2013, the company also issued 2,000 6% debentures of ₹100 each at a discount of 4% redeemable at a premium of 5% in four equal annual instalments beginning from the second year of the issue.

The company had a balance of ₹1,00,000 in its General Reserve on 31st March, 2014.

You are required to show the items under the heading Equity and Liabilities in the Balance Sheet of the company as on 31st March, 2014 (as per Schedule III, showing clearly Notes to Accounts). Ignore interest on debentures. Loss on issue of debentures is to be written off in the first year itself. *(I.S.C. Sample Question Paper, 2015)*

SOLUTION : **Newtown Ltd.**

EXTRACT OF BALANCE SHEET *as at 31st March, 2014*

Particulars	*Note No.*	*31st March, 2014*	*31st March, 2013*
		₹	₹
I. EQUITY AND LIABILITIES :			
(1) **Shareholder's Funds :**			
(*a*) Share Capital	1	6,48,000	
(*b*) Reserve and Surplus	2	82,000	
(2) **Non-Current Liabilities :**			
(*a*) Long-term Borrowings	3	2,10,000	
		9,40,000	

Notes to Accounts :

Particulars			₹
(1) **Share Capital :**			
Authorised Capital :			
1,00,000 Equity Shares of ₹10 each			10,00,000
Issued Capital :			
70,000 Equity Shares of ₹10 each			7,00,000
Subscribed and Fully Paid Capital :			
64,000 Equity Shares of ₹10 each fully Called up		6,40,000	
Subscribed but not Fully Paid Capital :			
400 Equity Shares of ₹10 each fully Called up	4,000		
Less : Calls in Arrears (400 Shares × ₹2)	800	3,200	
		6,43,200	
Add : Share Forfeited A/c (600 Shares × ₹8)		4,800	6,48,000
(2) **Reserve and Surplus :**			
General Reserve		1,00,000	
Less : Loss on Issue written off			
Discount on Issue	8,000		
Premium on Redemption	10,000	18,000	82,000
(3) **Long term Borrowings :**			
2,000, 6% Debentures of ₹100 each		2,00,000	
Premium on Redemption of Debentures		10,000	2,10,000

Multiple Choice Questions

Select the Best Alternate and tally your answer with the Answers given at the end of the book :

Q. 1. Debenture holders are :

(A) Owners of the Company (B) Debtors of the Company

(C) Creditors of the Company (D) Promoters of the Company

Q. 2. Debentures represent the :

(A) Long-term Borrowings of a Company
(B) The Investment of Equity-Shareholders
(C) Directors' shares in a company
(D) Short-term Borrowings of a Company

Q. 3. Zero Coupon Bonds are issued :

(A) At Zero Interest Rate
(B) With Specified Rate of Interest
(C) Without Specified Rate of Interest
(D) None of These

Q. 4. Interest payable on debentures is :

(A) an appropriation of profits of the company
(B) a charge against profits of the company
(C) transferred to sinking fund investment account
(D) transferred to general reserve

Q. 5. A debenture holder is entitled to :

(A) Fixed dividend (B) Share in profits
(C) Voting rights in the company (D) Interest at the fixed rate

Q. 6. On liquidation of company, principal amount of debentures is returned :

(A) First of All (B) Last of All
(C) Before Equity Capital (D) After Equity Capital

Q. 7. Which of the following statements is false?

(A) Debenture is a form of public borrowing.
(B) It is customary to prefix debentures with the agreed rate of interest.
(C) Debenture interest is a charge against profits.
(D) The issue price and redemption value of debentures cannot differ.

Q. 8. Which of the following is not a characteristic of Bearer Debentures?

(A) They are treated as negotiable instruments.
(B) Their transfer requires a deed of transfer.
(C) They are transferable by mere delivery.
(D) The interest on it is paid to the holder irrespective of identity.

HOTS

Q. 9. Which of the following statements is false?

(A) At maturity, debenture holders get back their money.
(B) Debentures can be forfeited for non-payment of call money.
(C) In company's balance sheet, debentures are shown under the head Long term Borrowings.
(D) Interest on debentures is a charge against profits.

HOTS

Q. 10. Which of the following statements is false :

(A) A Company can issue redeemable debentures.
(B) A Company can issue debentures with voting rights.
(C) A Company can issue convertible debentures.
(D) A Company can buy its own debentures and shares.

Q. 11. The Principal amount of debentures will be repaid by the company either at the end of a specified period or by instalments during the life time of the company. Such types of debentures are called :

(A) Redeemable Debentures
(B) Irredeemable Debentures
(C) Convertible Debentures
(D) Bearer Debentures

Q. 12. The debentures whose principal amount is not repayable by the company during its life time, but the payment is made only at the time of Liquidation of the company, such debentures are called :

(A) Bearer Debentures
(B) Redeemable Debentures
(C) Irredeemable Debentures
(D) Non-Convertible Debentures

Q. 13. Debenture Application Account is in the nature of

(A) Real Account
(B) Personal Account
(C) Nominal Account
(D) None of the above

Q. 14. Discount on issue of Debentures is in the nature of

(A) Revenue loss
(B) Capital loss
(C) Deferred Revenue Expenditure
(D) None of the above

Q. 15. Premium received on issue of debentures may be utilised for

(A) For writing off discount allowed on issue of shares

(B) For writing off premium allowed on redemption of debentures

(C) For writing off preliminary expenses

(D) All of the Above

Q. 16. '*A*' Limited purchased the assets from '*B*' Limited for ₹5,40,000. '*A*' Limited issued 10% debentures of ₹100 each at 10% discount against the payment. The number of debentures received by '*B*' Limited will be :

(A) 54,000
(B) 5,400
(C) 60,000
(D) None of the above

Q. 17. '*A*' Limited purchased the assets from '*B*' Limited for ₹5,40,000. '*A*' Limited issued 10% debentures of ₹100 each at 20% premium against the payment. The number of debentures received by '*B*' Limited will be :

(A) 4,500
(B) 5,400
(C) 45,000
(D) 6,000

Q. 18. '*A*' Limited purchased the assets from '*B*' Limited for ₹8,10,000. '*A*' Limited issued 10% debentures of ₹100 each at 10% discount against the payment. The number of debentures received by '*B*' Limited will be :

(A) 8,100 (B) 9,000
(C) 90,000 (D) None of the above

Q. 19. Debentures of a Company can be issued :

(A) For Cash
(B) For Consideration other than Cash
(C) As a Collateral Security
(D) Any of the above

Q. 20. On issue of debentures as a collateral security, which account is credited?

(A) Debentures Account
(B) Bank Loan Account
(C) Debenture Holdings Account
(D) Debenture Suspense Account

Q. 21. Debentures issued as collateral security will be debited to :

(A) Bank Account
(B) Debentures Suspense Account
(C) Debentures Account
(D) Bank Loan Account

HOTS

Q. 22. When debentures of ₹1,00,000 are issued as Collateral Security against a loan of ₹1,50,000, the entry for issue of debentures will be :

(A) Credit Debentures ₹1,50,000 and debit bank A/c ₹1,50,000
(B) Debit Debenture Suspense A/c ₹1,00,000 and Credit Bank A/c ₹1,00,000
(C) Debit Debenture Suspense A/c ₹1,00,000 and Credit Debentures A/c ₹1,00,000.
(D) Debit Cash A/c ₹1,50,000 and Credit Bank A/c ₹1,50,000

HOTS

Q. 23. Interest on debentures issued as a collateral security is paid on :

(A) Nominal value of debentures (B) No interest is paid
(C) Face value of debentures (D) Paid up value of debentures

Q. 24. When debentures are to be redeemed at premium an extra entry has to be made at the time of issue of debentures, which a/c should be credited in this entry?

(A) Loss on issue of debentures a/c
(B) Debenture redemption premium a/c
(C) Bank a/c
(D) Debenture holder's a/c

Q. 25. Premium on Redemption of Debentures Account is :

(A) Personal Account
(B) Real Account
(C) Nominal Account
(D) All of the Above

Q. 26. *X* Ltd. acquired assets of ₹20 lakhs and took over creditors of ₹20 thousand from *Y* Ltd. *X* Ltd. issued 8% debentures of ₹200 each at a discount of 10% as purchase consideration. Number of debentures issued will be :

(A) 11,000
(B) 9,000
(C) 10,000
(D) 10,100

Q. 27. *X* Ltd. purchased a building for ₹60,00,000 payable as 20% in Cash and balance by allotment of 8% debentures of ₹500 each at a premium of 20%. Number of debentures issued will be :

(A) 9,600
(B) 8,000
(C) 12,000
(D) 10,000

Q. 28. Sunrise Ltd. purchased a building for ₹5,00,000 payable as 15% in cash and balance by allotment of 9% debentures of ₹100 each at a premium of 25%. Number of debentures issued will be :

(A) 4,250
(B) 4,000
(C) 5,000
(D) 3,400

Q. 29. If Vendors are issued debentures of ₹80,000 in consideration of net assets of ₹1,00,000, the balance of ₹20,000 will be credited to :

(A) Statement of Profit & Loss
(B) Goodwill Account
(C) General Reserve Account
(D) Capital Reserve Account

Q. 30. If Vendors are issued debentures of ₹4,40,000 in consideration of assets of ₹5,00,000 and liabilities of ₹1,00,000, the balance of ₹40,000 will be debited to:

(A) General Reserve Account
(B) Capital Reserve Account
(C) Goodwill Account
(D) Statement of Profit & Loss

Q. 31. A Ltd. issued 1,000, 10% debentures of ₹100 each at a premium of 5%. What will be the total amount of interest for one year?

(A) ₹10,500
(B) ₹10,000
(C) ₹ 5,250
(D) ₹ 5,000

Q. 32. On 1st April 2021, Sunrise Limited issued 5,000, 8% debentures of ₹100 each at a discount of 5%. What will be the total amount of interest for the year ending 31st March 2022?

(A) ₹38,000
(B) ₹42,000
(C) ₹40,000
(D) ₹25,000

Q. 33. Globe Ltd. issues 20,000, 9% debentures of ₹100 each at a discount of 5% redeemable at the end of 5 years at a premium of 6%. For what amount 'Loss on Issue of Debentures Account' will be debited?

(A) ₹1,00,000
(B) ₹1,20,000
(C) ₹2,80,000
(D) ₹2,20,000

Q. 34. Issued 5,000, 12% debentures of ₹100 each at a discount of 2%, redeemable at a premium of 5%. In such case :

(A) Loss on Issue will be Credited by ₹10,000.

(B) Loss on Issue will be debited by ₹35,000.

(C) Premium on Redemption will be debited by ₹25,000.

(D) Premium on Redemption will be credited by ₹35,000.

Q. 35. Issued 4,000, 12% debentures of ₹100 each at a premium of 4%, redeemable at a premium of 10%. In such case :

(A) Loss on Issue will be debited by ₹24,000

(B) Loss on Issue will be debited by ₹56,000

(C) Loss on Issue will be debited by ₹40,000

(D) Premium on Redemption will be credited by ₹24,000

Q. 36. When debentures are to be redeemed at premium, an extra entry has to be made at the time of issue of debentures, which A/c should be debited in this entry?

(A) Loss on issue of debentures A/c

(B) Debenture Redemption Premium A/c

(C) Bank A/c

(D) Debenture holder's A/c

Q. 37. Issued 10,000, 8% debentures of ₹100 each at a premium of 3%, redeemable at a premium of 5%. In such case :

(A) Loss on Issue will be debited by ₹20,000

(B) Loss on Issue will be debited by ₹80,000

(C) Loss on Issue will be debited by ₹50,000

(D) Premium on Redemption will be credited by ₹20,000

(See answers at the end of the book.)

8

Company Accounts — Redemption of Debentures

LEARNING OBJECTIVES

After studying this Chapter you should be able to understand :

- **Meaning of Redemption of Debenture**
- **Sources of Finance for the Redemption of Debentures**
  - **— Redemption of Debentures out of Capital**
  - **— Redemption of Debentures out of Profits**
  - **— Redemption of Debentures out of Capital and Profits**
- **Methods of Redemption of Debentures**
  - **(1) Lump-sum Payment at the end of Stipulated Period**
  - **(2) By Payment in Instalments by Draw of Lots**
  - **(3) By the Purchase of Own Debentures in the Open Market**

Meaning of Redemption of Debentures :

Redemption of debentures means repayment of the amount of debentures to debentureholders. In other words, redemption refers to discharge of liability on account of debentures by repaying the due amount of debentures. The terms and conditions of redemption are stated in the prospectus inviting applications for the issue of debentures. The terms of redemption are also clearly stated in the debenture certificate. Hence, the redemption is made in accordance with the terms of issue.

Sources of Finance for the Redemption of Debentures

Amount required for the redemption of debentures may be managed by a Company from the following sources :

(1) Redemption of Debentures out of Capital.

(2) Redemption of Debentures out of Profits.

(3) Redemption of Debentures out of Capital and Profits

(1) Redemption of Debentures out of Capital : When no profits are set aside for redemption of debentures it is called redemption out of Capital. In such a case no profits are transferred to Debenture Redemption Reserve.

In view of Section 71 (4) of the Companies Act 2013 and the Securities and Exchange Board of India (SEBI) guidelines requiring creation of Debenture Redemption Reserve are as follows :

(*i*) Listed companies are not required to create any Debenture Redemption Reserve. Hence, they can redeem all the debentures out of capital. (A listed company is a company whose shares are freely traded on a stock exchange.)

(*ii*) Unlisted companies are required to create Debenture Redemption Reserve equal to atleast 10% of the nominal (face) value of outstanding debentures out of divisible profits*. Hence, they can redeem 90% of their debentures out of capital.

* Divisible Profits means profits available for payment of dividend. As per Section 123 of Companies Act, 2013 Dividend can be paid by a company first out of current year's profits *i.e.* Surplus in Statement of Profit & Loss and in the event of inadequacy or absence of profits in any financial year, a Company may declare dividend out of dividend equalisation reserve and free reserves such as general reserve. Thus Debenture Redemption Reserve should be created first out of 'Surplus in Statement of Profit & Loss' and then out of Dividend Equalisation Reserve and General Reserve.

(2) Redemption of Debentures out of Profits : Redemption out of profits means that an amount equal to debentures outstanding (*i.e.*, 100% of the nominal (face) value of outstanding debentures) is transferred from divisible profits to a newly opened account named 'Debenture Redemption Reserve Account'. It is called redemption out of profits because the transfer of profit to Debenture Redemption Reserve (DRR) reduces the amount of profit available for dividend. It means that the profits set aside for DRR is not available for payment as dividend but would be utilised to redeem the debentures. Thus existing liquid resources of the Company are not affected by redemption in this manner.

(3) Redemption of Debentures Out of Capital and Profits : It means redemption of debentures partly out of capital and partly out of profits. For example, if an unlisted company creates DRR equivalent to 10% of outstanding debentures, then 10% redemption will be called out of profits and 90% redemption will be out of capital.

SEBI Guidelines for redemption of debentures :

(*i*) The creation of Debenture Redemption Reserve (*i.e.*, DRR) is obligatory only for non-convertible debentures and non-convertible portion of partly convertible debentures.

(*ii*) An unlisted company shall create DRR equivalent to at least 10% of the nominal (face) value of outstanding debentures.

Exemptions to the Rule of Creating DRR :

Following categories of companies are exempt from creating DRR : (For both Public as well as Privately Placed Debentures)

1. All India Financial Institutions, regulated by Reserve Bank of India (RBI).
2. Banking Companies.
3. Other Financial Institutions within the meaning of Section 2(72) of the Companies Act, 2013.
4. Listed Companies including :
    (*a*) Non-Banking Financing Companies (NBFCs), registered with RBI.
    (*b*) Housing Finance Companies (HFCs), registered with National Housing Bank.
    (*c*) Other Listed Companies.
5. Unlisted Non-Banking Financing Companies registered with RBI. (For Privately Placed Debentures)
6. Unlisted Housing Finance Companies registered with National Housing Bank. (For Privately Placed Debentures).

> Thus, only Unlisted Companies (other than NBFCs and HFCs) are required to create DRR equivalent to at least 10% of the nominal (face) value of outstanding debentures.

Debenture Redemption Reserve is shown on the Equity and Liabilities part of the Balance Sheet under the head **'Shareholders' Funds'** and sub-head **'Reserves and Surplus'**. On redemption of debentures, the amount proportionate to the debentures redeemed shall be transferred from Debenture Redemption Reserve (DRR) to General Reserve. For example, if the amount of outstanding debentures is ₹20,00,000 and there is a DRR of ₹2,00,000, then if 40% *i.e.,* ₹8,00,000 debentures are redeemed, 40% of ₹2,00,000 *i.e.,* ₹80,000 shall be transferred to General Reserve.

Debenture Redemption Reserve A/c ...Dr.
To General Reserve A/c

Condition of Investing 15% of the nominal (face) value of debentures maturing during the year :

As per Rule 18 (7) (b) of the Companies (Share Capital and Debentures) Rules 2014 (as amended) prescribes that all listed as well as unlisted Companies that are to redeem debentures, except the exempted Companies, shall before the 30th day of April of each year, deposit or invest in specified securities, a sum which shall not be less than 15% of the nominal (face) value of debentures maturing (to be redeemed) during the year ending on the 31st March of the next year.

For example, if a Company is to redeem debentures of ₹20,00,000 on 31st October, 2018, it must invest on or before 30th April, 2018 at least ₹3,00,000 (*i.e.,* 15% of ₹20,00,000) in specified securities.

The amount so deposited or invested can be utilized only for the purpose of repayment of debentures maturing during the year.

Exemptions to the Rule of depositing or investing 15% amount in specified securities :

Following categories of Companies are exempt from making debenture redemption investment (DRI) : (For both Public as well as Privately Placed Debentures)

1. All India Financial Institutions, regulated by Reserve Bank of India (RBI).
2. Banking Companies.
3. Other Financial Institutions within the meaning of Section 2 (72) of the Companies Act, 2013.
4. Unlisted Non-Banking Financing Companies registered with RBI. (For Privately Placed Debentures)
5. Unlisted Housing Finance Companies registered with National Housing Bank. (For Privately Placed Debentures)

Thus, following companies are required to deposit or invest at least 15% of the nominal or face value of its debentures maturing during the year :

(*i*) Listed Companies (including NBFCs registered with RBI and HFCs registered with National Housing Bank).

(*ii*) Unlisted Companies (other than NBFCs and NFCs mentioned above)

Explanation : It means that although Listed Companies are not required to create DRR, they must also invest atleast 15% of the debentures maturing during the year.

Methods of Redemption of Debentures

Following are the methods of redemption of debentures :

1. Lump-sum payment at the end of fixed period
2. Redemption of Debentures in instalments (By draw of lots)
3. By the purchase of own debentures from the open market
4. By conversion into shares or new debentures

It may be noted that Method No. 4 *i.e.* conversion into shares or new debentures is not in syllabus. Hence, it has not been discussed.

(1) Lump-sum payment at the end of fixed period : Under this method, the Company redeems whole of its debentures in one lump-sum at the expiry of a specified period, *i.e.*, at maturity date of the debentures or earlier at the option of the company. Such redemption may be made at par or at premium, according to the terms of issue.

As mentioned earlier it is necessary for an unlisted company to transfer an amount equal to 10% of the face value of debentures outstanding from 'Divisible Profits' to a newly opened account called "Debenture Redemption Reserve A/c" before the commencement of redemption of debentures. The effect of such a transfer is that it reduces the balance of profits, which ultimately reduces the amount available for dividends. The amount thus saved because of non-payment of dividends is utilized for the payment of debentures. Such redemption is called redemption out of profits because it reduces the amount of profits available for dividends. Such redemption does not affect the financial position of the Company adversely.

When all the debentures are redeemed in lump-sum, the Debenture Redemption Reserve A/c is closed by transferring its entire amount to General Reserve A/c.

The journal entries in this method are as follows :

(*i*) On 31st March of the previous year :

On transfer of profits by an unlisted Company @ 10% of the **face value of debentures outstanding :**

Surplus in Statement of Profit & Loss Dr.
Dividend Equalisation Reserve A/c Dr.
General Reserve A/c Dr.
To Debenture Redemption Reserve A/c

Note : In the absence of information only the 'Surplus in Statement of Profit & Loss' will be debited in this entry.

(*ii*) At the beginning of financial year (Upto 30th April) :

On making Investment by all unlisted as well as listed Companies @15% of the **face value of debentures to be redeemed :**

Debenture Redemption Investment A/c Dr.
To Bank A/c

(*iii*) At the time of redemption :

On Encashing Investment

Bank A/c Dr.
To Debenture Redemption Investment A/c

(*iv*) On redemption of debentures :

(*a*) Debentures A/c Dr.
To Debentureholders A/c

(*b*) Debentureholders A/c Dr.
To Bank A/c

(*v*) On transfer of amount of DRR to General Reserve :

Debenture Redemption Reserve (DRR) A/c Dr.
To General Reserve A/c

ILLUSTRATION 1. (Issue and Redemption of Debentures)

Saraswati Ltd. (an unlisted company) issued 10,000 6% Debentures of ₹100 each at a premium of 5% on 1st April, 2015 redeemable on March 31, 2020. The issue was fully subscribed. It was decided to invest 15% of the face value of debentures to be redeemed towards Debenture Redemption Investment on 30th April, 2019. Investments were encashed and Debentures were redeemed on due date. Record necessary entries for issue and redemption of debentures.

SOLUTION :

Books of Saraswati Ltd.

JOURNAL

Date	Particulars	L.F.	Dr. (₹)	Cr. (₹)
2015 April 1	Bank A/c Dr. To 6% Debenture Application & Allotment A/c (Receipt of application money)		10,50,000	 10,50,000
April 1	6% Debenture Application & Allotment A/c Dr. To 6% Debentures A/c To Securities Premium Reserve A/c (Transfer of application money)		10,50,000	 10,00,000 50,000
2019 March 31	Surplus in Statement of Profit & Loss Dr. To Debenture Redemption Reserve A/c (Transfer of profits equal to 10% of the nominal value of debentures outstanding)		1,00,000	 1,00,000
April 30	Debenture Redemption Investment Dr. To Bank A/c (Investment made @15% of the face value of debentures to be redeemed)		1,50,000	 1,50,000
2020 March 31	Bank A/c Dr. To Debenture Redemption Investment A/c (Investment encashed)		1,50,000	 1,50,000
March 31	6% Debentures A/c Dr. To Debentureholder's A/c (Amount due on redemption)		10,00,000	 10,00,000
March 31	Debentureholder's A/c Dr. To Bank A/c (Payment of amount due to debentureholders)		10,00,000	 10,00,000
March 31	Debenture Redemption Reserve A/c Dr. To General Reserve A/c (Transfer of Debenture Redemption Reserve A/c to General Reserve A/c on redemption)		1,00,000	 1,00,000

Notes : (1) DRR will be created @ 10% of the nominal (face) value of outstanding debentures on 31st March of the previous year.

(2) DRR will be created only by an unlisted company. An unlisted company is a company whose shares are not traded on a stock exchange.

(3) Minimum investment of 15% of the nominal (face) value of debentures maturing during the year will be made by all unlisted as well as listed companies on or before 30th April of the year in which debentures are to be redeemed and the same will be encashed at the time of redemption of debentures.

(4) Interest on Investment is not calculated because rate of interest is not given.

(5) There is no need to pass entries for interest on debentures unless required.

ILLUSTRATION 2

(Issue and Redemption of Debentures)

Tulip Ltd. (an unlisted company) issued ₹4,00,000, 9% Debentures of ₹100 each on April 1, 2016 at a premium of 6%, redeemable at a premium of 10% on 31st March, 2020. Assume that required investment was made in 10% Government Securities on April 30 of the financial year in which redemption is due. Debentures were redeemed on the due date.

Pass journal entries at the time of Issue and Redemption of Debentures.

SOLUTION

Books of Tulip Ltd.

JOURNAL

Date	*Particulars*		*L.F.*	*Dr. (₹)*	*Cr. (₹)*
2016					
April 1	Bank A/c	Dr.		4,24,000	
	To 9% Debenture Application & Allotment A/c				4,24,000
	(Receipt of application money)				
April 1	9% Debenture Application & Allotment A/c	Dr.		4,24,000	
	Loss on Issue of Debentures A/c	Dr.		40,000	
	To 9% Debentures A/c				4,00,000
	To Securities Premium Reserve A/c				24,000
	To Premium on Redemption of Debentures A/c				40,000
	(Transfer of application money)				
2019					
March 31	Surplus in Statement of Profit & Loss	Dr.		40,000	
	To Debenture Redemption Reserve A/c				40,000
	(Transfer of profits equal to 10% of the nominal value of debentures outstanding)				
April 30	Debenture Redemption Investment A/c	Dr.		60,000	
	To Bank A/c				60,000
	(Investment made @15% of the face value of debentures to be redeemed)				
2020					
March 31	Bank A/c	Dr.		65,500	
	To Debenture Redemption Investment A/c				60,000
	To Interest Received A/c				*5,500
	(Investment bearing 10% p.a. interest encashed)				
March 31	9% Debentures A/c	Dr.		4,00,000	
	Premium on Redemption of Debentures A/c	Dr.		40,000	
	To Debentureholder's A/c				4,40,000
	(Amount due on redemption)				
March 31	Debentureholder's A/c	Dr.		4,40,000	
	To Bank A/c				4,40,000
	(Payment of amount due to debentureholders)				

March 31	Debenture Redemption Reserve A/c Dr. To General Reserve A/c (Transfer of Debenture Redemption Reserve A/c to General Reserve A/c on redemption)		40,000	40,000
March 31	Interest Received A/c Dr. To Statement of Profit & Loss (Transfer of interest on investments)		5,500	5,500

* Interest is calculated for 11 months.

ILLUSTRATION 3.

(Redemption of Debentures in case of Banking Company)

State Bank of India issued 20,000, 6% Debentures of ₹50 each at a premium of 8% on June 30, 2010 redeemable on June 30, 2020. The issue was fully subscribed. Record necessary entries for issue and redemption of debentures.

SOLUTION :

Books of State Bank of India

JOURNAL

Date	*Particulars*	*L.F.*	*Dr.* (₹)	*Cr.* (₹)
2010 June 30	Bank A/c Dr. To 6% Debenture Application & Allotment A/c (Receipt of application money)		10,80,000	10,80,000
June 30	6% Debenture Application & Allotment A/c Dr. To 6% Debentures A/c To Securities Premium Reserve A/c (Transfer of application money)		10,80,000	10,00,000 80,000
2020 June 30	6% Debentures A/c Dr. To Debentureholders A/c (Amount due on redemption)		10,00,000	10,00,000
June 30	Debentureholders A/c Dr. To Bank A/c (Payment of amount due to debentureholders)		10,00,000	10,00,000

Notes : (1) As per Section 71 (4) with rule 18 (7) a Banking Company is not required to create Debenture Redemption Reserve.

(2) A banking Company is exempted from investing 15% amount.

ILLUSTRATION 4.

On 1st April 2015, Godrej Ltd., which is **listed on the stock exchange**, issued 20,000, 8% Debentures of ₹100 each at a discount of 4%, redeemable at a premium of 5% after 5 years. The issue was fully subscribed. Debentures were redeemed on due date. Pass necessary entries for issue and redemption of debentures, assuming that the loss on issue was written off at the end of first year.

SOLUTION :

Books of Godrej Ltd.

JOURNAL

Date	*Particulars*		*L.F.*	*Dr. (₹)*	*Cr. (₹)*
2015					
April 1	Bank A/c	Dr.		19,20,000	
	To Debenture Application and Allotment A/c				19,20,000
	(Application and allotment money received on issue of Debentures)				
April 1	Debenture Application and Allotment A/c	Dr.		19,20,000	
	Loss on Issue of Debentures A/c	Dr.		1,80,000	
	To 8% Debentures A/c				20,00,000
	To Premium on Redemption of Debentures A/c				1,00,000
	(Allotment of Debentures redeemable at 5% premium)				
2016					
March 31	Statement of Profit & Loss	Dr.		1,80,000	
	To Loss on Issue of Debentures A/c				1,80,000
	(Loss on issue written off)				
2019					
April 30	Debenture Redemption Investment A/c	Dr.		3,00,000	
	To Bank A/c				3,00,000
	(Investment made @15% of the face value of debentures to be redeemed)				
2020					
March 31	Bank A/c	Dr.		3,00,000	
	To Debenture Redemption Investment A/c				3,00,000
	(Investment encashed)				
March 31	8% Debentures A/c	Dr.		20,00,000	
	Premium on Redemption of Debentures A/c	Dr.		1,00,000	
	To Debentureholder's A/c				21,00,000
	(Amount due to Debentureholders)				
March 31	Debentureholder's A/c	Dr.		21,00,000	
	To Bank A/c				21,00,000
	(Amount paid on redemption)				

Note : There is no requirement of creation of DRR in case of a listed company. However, such Companies are also required to make minimum investment of 15% of debentures to be redeemed.

ILLUSTRATION 5.

Alpha Ltd. (an unlisted company) has 10,000, 8% Debentures of ₹100 each due for redemption on 31st March 2022. Debenture Redemption Reserve has a balance of ₹40,000 on 31st March, 2021. It was decided to invest the required amount towards Debenture Redemption Investment. Investments were realised at 104% less 0.5% brokerage and debentures were redeemed. Record the necessary entries for the redemption of debentures.

SOLUTION :

Books of Alpha Ltd.

JOURNAL

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
2021 March 31	Surplus in Statement of Profit and Loss[2]	Dr.		60,000	
	To Debenture Redemption Reserve A/c				60,000
	(Transfer of profits as per SEBI guidelines)				
April 30	Debenture Redemption Investment A/c	Dr.		1,50,000	
	To Bank A/c				1,50,000
	(Investment made @15% of the face value of debentures to be redeemed)				
2022 March 31	Bank A/c[1]	Dr.		1,55,220	
	To Debenture Redemption Investment A/c				1,50,000
	To Profit on Sale of Investments A/c				5,220
	(Investment encashed at 104% *less* brokerage 0.5%)				
March 31	Profit on Sale of Investment A/c	Dr.		5,220	
	To Statement of Profit & Loss				5,220
	(Transfer of profit on sale of investments)				
March 31	8% Debentures A/c	Dr.		10,00,000	
	To Debentureholders A/c				10,00,000
	(Amount due on redemption)				
March 31	Debentureholders A/c	Dr.		10,00,000	
	To Bank A/c				10,00,000
	(Payment of amount due to debentureholders)				
March 31	Debenture Redemption Reserve A/c	Dr.		1,00,000	
	To General Reserve A/c				1,00,000
	(Transfer of Debenture Redemption Reserve A/c to General Reserve A/c on redemption)				

Working Note :

(1) Amount realised from sale of investments :

		₹
$1{,}50{,}000 \times \frac{104}{100}$	=	1,56,000
Less : Brokerage $1{,}56{,}000 \times \frac{0.5}{100}$	=	780
		1,55,220

(2) Total Amount required for transfer to

		₹
Debenture Redemption Reserve = 10% of 10,00,000	=	1,00,000
Less : Existing Balance	=	40,000
Amount now required to be transferred to Debenture Redemption Reserve		60,000

ILLUSTRATION 6.

Mahesh Ltd. (an unlisted company) had issued 20,000, 10% debentures of ₹100 each out of which, 8,000, 10% debentures were due for redemption on 31st March, 2019. The company had a balance of ₹1,40,000 in the Debenture Redemption Reserve

Account on 31st March, 2018. The company invested the required amount in the Debenture Redemption Investment on 1st April, 2018.

Pass the necessary journal entries for redemption of debentures. Ignore the entries for interest on debentures. *(C.B.S.E. 2020, Mumbai, Chennai)*

SOLUTION :

Books of Mahesh Ltd.

JOURNAL

Date	*Particulars*		*L.F.*	*Dr.* (₹)	*Cr.* (₹)
2018 March 31	Surplus in Statement of Profit and Loss⁽¹⁾	Dr.		60,000	
	To Debenture Redemption Reserve A/c				60,000
	(Transfer of profits to Debenture Redemption Reserve)				
April 1	Debenture Redemption Investment A/c	Dr.		1,20,000	
	To Bank A/c				1,20,000
	(Investment made @15% of the face value of debentures to be redeemed *i.e.* 15% of ₹8,00,000)				
2019 March 31	Bank A/c	Dr.		1,20,000	
	To Debenture Redemption Investment A/c				1,20,000
	(Investment encashed)				
March 31	10% Debentures A/c	Dr.		8,00,000	
	To Debentureholders A/c				8,00,000
	(Amount due to debentureholders on redemption of debentures)				
March 31	Debentureholders A/c	Dr.		8,00,000	
	To Bank A/c				8,00,000
	(Payment of amount due to debentureholders)				
March 31	Debenture Redemption Reserve A/c⁽²⁾	Dr.		80,000	
	To General Reserve A/c				80,000
	(Proportionate amount of DRR transferred to General Reserve on redemption of 8,000 debentures)				

Notes : (1)

	₹
Total amount required for transfer to Debenture Redemption Reserve = 10% of ₹20,00,000	2,00,000
Less : Existing Balance	1,40,000
Amount now required to be transferred to Debenture Redemption Reserve	60,000

(2) Total DRR for 20,000 Debentures = ₹2,00,000

$$\text{Proportionate DRR for 8,000 Debentures} = \frac{2,00,000}{20,000} \times 8,000 = ₹80,000$$

ILLUSTRATION 7.

On 1st April, 2017, KK Ltd. (an unlisted company) invited applications for issuing 5,000 10% debentures of ₹1,000 each at a discount of 6%. These debentures were repayable at the end of 3rd year at a premium of 10%. Applications for 6,000 debentures were received and the debentures were allotted on pro-rata basis to all the applicants. Excess money received with applications was refunded.

The directors decided to transfer the minimum amount to Debenture Redemption Reserve on 31.3.2019. On 1.4.2019, the company invested the necessary amount in 9% bank fixed deposit as per the provisions of the Companies Act, 2013. Tax was deducted at source by bank on interest @10%.

Pass the necessary journal entries for issue and redemption of debentures. Ignore entries relating to writing off loss on issue of debentures and interest paid on debentures.

SOLUTION :

Books of K.K. Ltd.

JOURNAL

Date	*Particulars*		*L.F.*	*Dr. (₹)*	*Cr. (₹)*
2017 April 1	Bank A/c	Dr.		56,40,000	
	To Debenture Application and Allotment A/c				56,40,000
	(Application and allotment money received, 6,000 × ₹940)				
April 1	Debenture Application and Allotment A/c	Dr.		56,40,000	
	Loss on Issue of Debentures A/c	Dr.		8,00,000	
	To 10% Debentures A/c				50,00,000
	To Premium on Redemption of Debentures A/c				5,00,000
	To Bank A/c				9,40,000
	(Allotment of Debentures redeemable at 10% premium)				
2019 March 31	Surplus *i.e.,* Balance in Statement of Profit & Loss	Dr.		5,00,000	
	To Debenture Redemption Reserve A/c				5,00,000
	(Transfer of profit equal to 10% of ₹50,00,000)				
April 1	Debenture Redemption Investment A/c	Dr.		7,50,000	
	To Bank A/c				7,50,000
	(Investment made @ 15% of ₹50,00,000)				
2020 March 31	Bank A/c	Dr.		8,10,750	
	TDS Deposited A/c	Dr.		6,750	
	To Debenture Redemption Investment A/c				7,50,000
	To Interest Received A/c				67,500
	(Fixed deposit encashed on Redemption)				
March 31	10% Debentures A/c	Dr.		50,00,000	
	Premium on Redemption of Debentues A/c	Dr.		5,00,000	
	To Debentureholder's A/c				55,00,000
	(Amount due to Debentureholders)				
March 31	Debentureholder's A/c	Dr.		55,00,000	
	To Bank A/c				55,00,000
	(Amount paid on redemption)				

March 31	Debenture Redemption Reserve A/c Dr. To General Reserve A/c (Debenture Redemption Reserve transferred to General Reserve)		5,00,000	5,00,000
March 31	Interest Received A/c Dr. To Statement of Profit & Loss (Transfer of interest on investments)		67,500	67,500

ILLUSTRATION 8.

X Ltd. (an unlisted company) had issued ₹10,00,000, 9% debentures which are due to be redeemed out of profits on 1st October 2020 at a premium of 5%. The company had a Debenture Redemption Reserve of ₹4,14,000. It was decided to invest the required amount in Debenture Redemption Investment. Pass necessary journal entries for the redemption of debentures.

SOLUTION :

Books of X Ltd.
JOURNAL

Date	*Particulars*	*L.F.*	*Dr.* (₹)	*Cr.* (₹)
2020 March 31	Surplus in Statement of Profit and Loss(2) Dr. To Debenture Redemption Reserve A/c (Transfer of profit to Debenture Redemption Reserve)		5,86,000	5,86,000
April 30	Debenture Redemption Investment A/c Dr. To Bank A/c (Investment made @15% of the face value of debentures to be redeemed)		1,50,000	1,50,000
Oct. 1	Bank A/c Dr. To Debenture Redemption Investment A/c (Investment encashed)		1,50,000	1,50,000
Oct. 1	9% Debentures A/c Dr. Premium on Redemption of Debentures A/c Dr. To Debentureholders A/c (Amount due on redemption)		10,00,000 50,000	10,50,000
Oct. 1	Debentureholders A/c Dr. To Bank A/c (Payment of amount due to debentureholders)		10,50,000	10,50,000
Oct. 1	Debenture Redemption Reserve A/c Dr. To General Reserve A/c (Transfer of Debenture Redemption Reserve A/c to General Reserve A/c on redemption)		10,00,000	10,00,000

Notes : (1) Since the debentures are to be redeemed purely out of profits, an amount equal to 100% of nominal value of debentures redeemed *i.e.*, ₹10,00,000 is transferred to Debenture Redemption Reserve. If such Reserve is created only with 10% of the total amount of debentures redeemed, it would mean that remaining 90% of the debentures have been redeemed out of capital.

		₹
(ii) Total Amount required for transfer to Debenture Redemption Reserve = 100% of 10,00,000	=	10,00,000
Less : Existing Balance	=	4,14,000
Amount now required to be transferred to Debenture Redemption Reserve		5,86,000

ILLUSTRATION 9.

Poonam Ltd. (an unlisted company) had a balance of ₹55,00,000 in its Statement of Profit and Loss. Instead of declaring a dividend it decided to redeem its ₹50,00,000, 8% debentures at a premium of 10% out of profits on 31st March, 2020. The Company invested the required amount in fixed deposit in a bank on 30th April, 2019 earning interest @8% p.a. Tax was deducted on interest earned @10% by the bank. Pass the necessary Journal entries in the books of the company for the redemption of debentures.

SOLUTION :

Books of Poonam Ltd.

JOURNAL

Date	*Particulars*		*L.F.*	*Dr. (₹)*	*Cr. (₹)*
2019 March 31	Surplus in Statement of Profit and Loss[(1)]	Dr.		50,00,000	
	To Debenture Redemption Reserve A/c				50,00,000
	(Transfer of profits to DRR)				
April 30	Debenture Redemption Investment A/c	Dr.		7,50,000	
	To Bank A/c				7,50,000
	(Investment made @15% of the face value of debentures to be redeemed)				
2020 March 31	Bank A/c	Dr.		7,99,500	
	TDS Deposited A/c	Dr.		5,500	
	To Debenture Redemption Investment A/c				7,50,000
	To Interest Received A/c				55,000
	(Fixed deposit earning interest @8% p.a. encashed on redemption)				
March 31	8% Debentures A/c	Dr.		50,00,000	
	Premium on Redemption of Debentures A/c	Dr.		5,00,000	
	To Debentureholders A/c				55,00,000
	(Amount due on redemption)				
March 31	Debentureholders A/c	Dr.		55,00,000	
	To Bank A/c				55,00,000
	(Payment of amount due to debentureholders)				
March 31	Debenture Redemption Reserve A/c	Dr.		50,00,000	
	To General Reserve A/c				50,00,000
	(Transfer of Debenture Redemption Reserve A/c to General Reserve A/c on redemption)				

March 31	Interest Received A/c Dr. To Statement of Profit and Loss (Transfer of interest on investments)		55,000	55,000

Note (1) Since the debentures are redeemable fully out of profits, an amount equal to the total amount of debentures redeemed *i.e.*, ₹50,00,000 (and not 10% of ₹50,00,000) has been transferred to Debenture Redemption Reserve.

ILLUSTRATION 10.

On 1st April, 2013, Rayon Ltd. (an unlisted company) issued 20,000, 9% Debentures of ₹100 each at a discount of 10%, redeemable at par on 31st March, 2017. The issue was fully subscribed. To meet the provisions of the Companies Act, 2013, the Board of Directors decided to transfer ₹1,20,000 to Debenture Redemption Reserve on 31st March, 2014, and the balance on 31st March, 2015. On 1st April, 2016, the company made the required investment in government securities.

The investments were encashed and the debentures were redeemed on the due date.

It is the policy of the company to write off capital losses in the year in which they occur.

You are required to pass journal entries for issue and redemption of debentures (ignore interest on debentures). *(I.S.C. 2018)*

SOLUTION :

JOURNAL OF RAYON LTD.

Date	*Particulars*	*L.F.*	*Dr.* (₹)	*Cr.* (₹)
2013 April 1	Bank A/c Dr. To 9% Debenture Application and Allotment A/c (Debenture application money received)		18,00,000	18,00,000
April 1	9% Debenture Application and Allotment A/c Dr. Discount on Issue of Debentures A/c Dr. To 9% Debentures A/c (Issue of Debentures at 10% discount)		18,00,000 2,00,000	20,00,000
2014 March 31	Statement of Profit and Loss Dr. To Discount on Issue of Debentures A/c (Discount on issue of debentures written off)		2,00,000	2,00,000
March 31	Surplus in Statement of Profit and Loss Dr. To Debenture Redemption Reserve A/c (Transfer of profits to DRR)		1,20,000	1,20,000
2015 March 31	Surplus in Statement of Profit & Loss(1) Dr. To Debenture Redemption Reserve A/c (Transfer of profits to DRR)		80,000	80,000

2016 April 1	Debenture Redemption Investment A/c Dr. To Bank A/c (Investment made @15% of the face value of debentures to be redeemed)		3,00,000	3,00,000
2017 March 31	Bank A/c Dr. To Debenture Redemption Investment A/c (Investment encashed)		3,00,000	3,00,000
March 31	9% Debentures A/c Dr. To Debentureholders' A/c (Amount due on redemption)		20,00,000	20,00,000
March 31	Debentureholders' A/c Dr. To Bank A/c (Payment made to Debentureholders)		20,00,000	20,00,000
March 31	Debenture Redemption Reserve A/c Dr. To General Reserve A/c (Transfer of DRR to General Reserve)		2,00,000	2,00,000

Note 1. Total amount required to be transferred to Debenture Redemption Reserve

= 10% of 20,00,000	= ₹ 2,00,000
Less : Transferred on 31st March, 2014	1,20,000
Balance amount to be transferred on 31st March, 2015	80,000

ILLUSTRATION 11.

Kusum Steel Industries Ltd. (an unlisted company) issued 21,000, 7½ % Debentures of ₹100 each on March 31, 2013 redeemable at a premium of 8% on 30th June, 2020. The Board of Directors decided to transfer the required amount to Debenture Redemption Reserve in three equal annual instalments starting with March 31, 2018. Record necessary journal entries regarding issue and redemption of debentures. Ignore entries relating to writing off loss on issue of debentures and interest paid thereon.

SOLUTION :

Books of Kusum Steel Industries Ltd.

JOURNAL

Date	*Particulars*	*L.F.*	*Dr.* (₹)	*Cr.* (₹)
2013	*At the time of issue*			
March 31	Bank A/c Dr. To 7½% Debenture Application & Allotment A/c (Application money received on issue of debentures)		21,00,000	21,00,000
March 31	7½% Debenture Application & Allotment A/c Dr. Loss on Issue of Debentures A/c Dr. To 7½ % Debentures A/c To Debenture Redemption Premium A/c (Transfer of application money)		21,00,000 1,68,000	21,00,000 1,68,000

2018 March 31	*For creation of Debenture Redemption Reserve* Surplus in Statement of Profit and Loss Dr. To Debenture Redemption Reserve A/c (Transfer of profits to Debenture Redemption Reserve)		70,000	70,000
2019 March 31	Surplus in Statement of Profit and Loss Dr. To Debenture Redemption Reserve A/c (Transfer of profits to Debenture Redemption Reserve)		70,000	70,000
2020 March 31	Surplus in Statement of Profit and Loss Dr. To Debenture Redemption Reserve A/c (Transfer of profits to Debenture Redemption Reserve)		70,000	70,000
April 30	Debenture Redemption Investment A/c Dr. To Bank A/c (Investment made @15% of the face value of debentures to be redeemed)		3,15,000	3,15,000
June 30	Bank A/c Dr. To Debenture Redemption Investment A/c (Investment encashed)		3,15,000	3,15,000
June 30	*At the time of redemption* 7½ % Debentures A/c Dr. Debentures Redemption Premium A/c Dr. To Debentureholders A/c (Amount due to debentureholders on redemption of debentures)		21,00,000 1,68,000	22,68,000
June 30	Debentureholders A/c Dr. To Bank A/c (Payment of amount due to debentureholders)		22,68,000	22,68,000
June 30	Debenture Redemption Reserve A/c Dr. To General Reserve A/c (Debenture Redemption Reserve transferred to General Reserve)		2,10,000	2,10,000

ILLUSTRATION 12 (A).

On 1st April, 2016, Ganesh Ltd. (an unlisted company) acquired assets of ₹6,00,000 and took over liabilities of ₹70,000 of Sohan Ltd. at an agreed value of ₹6,60,000. Ganesh Ltd. issued 12% Debentures of ₹100 each at a premium of 10% in full satisfaction of purchase consideration. Debentures were redeemable after three years at a premium of 5%. The company decided to transfer the minimum required amount to Debenture Redemption Reserve on 31st March, 2018. It also made the required investment in Government securities earning interest @ 10% p.a. on 1st April, 2018. Tax was deducted on interest earned @ 10%.

Ignoring entries relating to interest paid on debentures, pass the necessary journal entries to record the issue and redemption of debentures. *(C.B.S.E. 2019, Comptt.)*

SOLUTION:

JOURNAL OF GANESH LTD.

Date	Particulars	L.F.	Dr. (₹)	Cr. (₹)
2016 April 1	Sundry Assets A/c Dr.		6,00,000	
	Goodwill A/c (Balancing figure) Dr.		1,30,000	
	To Sundry Liabilities			70,000
	To Sohan Ltd.			6,60,000
	(Assets and liabilities acquired of Sohan Ltd.)			
,,	Sohan Ltd. Dr.		6,60,000	
	Loss on Issue of Debentures A/c Dr.		30,000	
	To 12% Debentures A/c(1)			6,00,000
	To Securities Premium Reserve A/c			60,000
	To Premium on Redemption of Debentures A/c			30,000
	(Debentures issued at a premium redeemable at a premium)			
2017 Mar. 31	Securities Premium Reserve A/c Dr.		30,000	
	To Loss on Issue of Debentures A/c			30,000
	(Loss on issue of debentures written off)			
2018 Mar. 31	Surplus i.e. balance in Statement of Profit and Loss (Note 2) Dr.		60,000	
	To Debenture Redemption Reserve A/c			60,000
	(Debenture Redemption Reserve created out of profits)			
April 1	10% Debenture Redemption Investments A/c Dr.		90,000	
	To Bank A/c			90,000
	(Debenture Redemption Investment purchased)			
2019 Mar. 31	Bank A/c Dr.		8,100	
	TDS Collected/Deposited A/c Dr.		900	
	To Interest on Debenture Redemption Investments A/c			9,000
	(Interest received on Debenture Redemption Investments)			
,,	Bank A/c Dr.		90,000	
	To 10% Debenture Redemption Investments A/c			90,000
	(Debenture Redemption Investments sold)			
	12% Debentures A/c Dr.		6,00,000	
	Premium on Redemption of Debentures A/c Dr.		30,000	
	To Debenture Holders A/c			6,30,000
	(Amount payable to debenture holders on redemption)			

,,	Debenture holders A/c Dr. To Bank A/c (Debentures redeemed)		6,30,000	6,30,000
,,	Interest on Debenture Redemption Investments A/c Dr. To Statement of Profit and Loss (Interest on Debenture Redemption Investments transferred to Statement of Profit and Loss)		9,000	9,000
,,	Debenture Redemption Reserve A/c Dr. To General Reserve A/c (Debenture Redemption Reserve transferred to general reserve)		60,000	60,000

Notes 1. Debentures issued = $\frac{6,60,000}{110}$ = 6,000 Debentures of ₹100 each.

2. An unlisted company is required to create Debenture Redemption Reserve (DRR) @ 10% of the outstanding debentures.

ILLUSTRATION 12(B)

Pass necessary Journal entries in the books of *X* Ltd. for the issue and redemption of Debentures in the following cases :

(*i*) 15,000; 10% Debentures of ₹100 each issued at 10% premium, repayable at par.

(*ii*) 6,000; 12% Debentures of ₹500 each issued at 5% premium, repayable at 10% premium.

Note : *X* Ltd. is an unlisted company.

SOLUTION : JOURNAL OF *X* LTD.

Date	*Particulars*	*L.F.*	*Dr.* (₹)	*Cr.* (₹)
(*i*)	**At the time of Issue of Debentures**			
	Bank A/c Dr. To 10% Debenture Application and Allotment A/c (Receipt of application money)		16,50,000	16,50,000
	10% Debenture Application and Allotment A/c Dr. To 10% Debentures A/c To Securities Premium Reserve A/c (Issue of Debentures at 10% premium, repayable at par)		16,50,000	15,00,000 1,50,000
	Before Redemption of Debentures Begins			
	Surplus in Statement of Profit and Loss Dr. To Debenture Redemption Reserve A/c (Amount transferred to DRR equal to 10% of the nominal value of debentures outstanding)		1,50,000	1,50,000

	Debenture Redemption Investment A/c To Bank A/c (Investment made @ 15% of the nominal value of debentures to be redeemed)	Dr.		2,25,000	2,25,000
	On Redemption Bank A/c To Debenture Redemption Investment A/c (Investments encashed)	Dr.		2,25,000	2,25,000
	10% Debentures A/c To Debentureholders' A/c (Amount due to debentureholders)	Dr.		15,00,000	15,00,000
	Debentureholders' A/c To Bank A/c (Amount paid to Debentureholders)	Dr.		15,00,000	15,00,000
	Debenture Redemption Reserve A/c To General Reserve A/c (Transfer of DRR to General Reserve after redemption)	Dr.		1,50,000	1,50,000
(*ii*)	**At the time of Issue of Debentures** Bank A/c To 12% Debenture Application and Allotment A/c (Receipt of application money)	Dr.		31,50,000	31,50,000
	12% Debenture Application and Allotment A/c Loss on Issue of Debentures A/c To 12% Debentures A/c To Securities Premium Reserve A/c To Premium on Redemption of Debentures A/c (Issue of debentures at 5% premium, repayable at 10% premium)	Dr. Dr.		31,50,000 3,00,000	30,00,000 1,50,000 3,00,000
	Securities Premium Reserve A/c Statement of Profit & Loss To Loss on Issue of Debentures A/c (Loss on issue of Debentures written off)	Dr. Dr.		1,50,000 1,50,000	3,00,000
	Before Redemption of Debentures Begins Surplus in Statement of Profit and Loss To Debenture Redemption Reserve A/c (Amount transferred to DRR equal to 10% of the nominal value of debentures outstanding)	Dr.		3,00,000	3,00,000
	Debenture Redemption Investment A/c To Bank A/c (Investment made @ 15% of the nominal value of debentures to be redeemed)	Dr.		4,50,000	4,50,000

	On Redemption Bank A/c Dr. To Debenture Redemption Investment A/c (Investments encashed)		4,50,000	4,50,000
	12% Debentures A/c Dr. Premium on Redemption of Debentures A/c Dr. To Debentureholders' A/c (Amount due to debentureholders)		30,00,000 3,00,000	33,00,000
	Debentureholders' A/c Dr. To Bank A/c (Amount paid to Debentureholders)		33,00,000	33,00,000
	Debenture Redemption Reserve A/c Dr. To General Reserve A/c (Transfer of DRR to General Reserve after redemption)		3,00,000	3,00,000

(2) Redemption of debentures in instalments by drawing of lots : According to this method, the debentures are redeemed in annual instalments. For example, the debentures for ₹10,00,000 may be redeemed at the rate of ₹2,00,000 per annum. The serial number of debentures which should be redeemed each year are selected by lottery. Debentures are redeemed at par or at a premium, according to the terms of issue. This procedure is known as "drawing by lots". Transfer of an amount equal to 10% of outstanding debentures to Debenture Redemption Reserve in case of an unlisted company before redemption begins is necessary in this method also.

It may be noted that proportionate amount of DRR will be transferred to General Reserve A/c in case of redemption in instalments.

ILLUSTRATION 13.

On 1st April 2018, Gomti Ltd. (an unlisted company) has 6,000, 8% debentures of ₹100 each due for redemption at 5% premium in three equal annual instalments starting from March 31, 2020. The Company complied with the requirements with respect to Investment made in Government Securities on 30th April, 2015.

Pass necessary journal entries and prepare ledger accounts.

SOLUTION :

Books of Gomti Ltd.

JOURNAL

Date	*Particulars*	*L.F.*	*Dr.* (₹)	*Cr.* (₹)
2019 March 31	Surplus in Statement of Profit and Loss Dr. To Debenture Redemption Reserve A/c (Transfer of profits to Debenture Redemption Reserve)		60,000	60,000

April 30	Debenture Redemption Investment A/c Dr. To Bank A/c (Investment made in Govt. Securities equal to 15% of the face value of debentures to be redeemed *i.e.* 15% of first instalment of ₹2,00,000)	30,000	30,000
2020 March 31	8% Debentures A/c Dr. Premium on Redemption of Debentures A/c Dr. To Debentureholders A/c (1/3rd of debentures and premium payable on redemption)	2,00,000 10,000	2,10,000
March 31	Debentureholders A/c Dr. To Bank A/c (Payment due to Debentureholders discharged)	2,10,000	2,10,000
March 31	Debenture Redemption Reserve A/c Dr. To General Reserve A/c (One-third amount of DRR transferred to general reserve on redemption of one-third debentures)	20,000	20,000
2021 March 31	8% Debentures A/c Dr. Premium on Redemption of Debentures A/c Dr. To Debentureholders A/c (1/3rd of debentures and premium payable on redemption)	2,00,000 10,000	2,10,000
March 31	Debentureholders A/c Dr. To Bank A/c (Payment due to Debentureholders discharged)	2,10,000	2,10,000
March 31	Debenture Redemption Reserve A/c Dr. To General Reserve A/c (One-third amount of DRR transferred to general reserve on redemption of one-third debentures)	20,000	20,000
2022 March 31	Bank A/c Dr. To Debenture Redemption Investment A/c (Investments encashed)	30,000	30,000
March 31	8% Debentures A/c Dr. Premium on Redemption of Debentures A/c Dr. To Debentureholders A/c (1/3rd of debentures and premium payable on redemption)	2,00,000 10,000	2,10,000

March 31	Debentureholders A/c Dr. To Bank A/c (Payment due to Debentureholders discharged)		2,10,000	2,10,000
March 31	Debenture Redemption Reserve A/c Dr. To General Reserve A/c (One-third amount of DRR transferred to general reserve on redemption of one-third debentures)		20,000	20,000

Note : In case of redemption in instalments, investment is made for first instalment and it remains invested till the last instalment. In this question, the Company has made investment on 30th April, 2019 which remains invested till the last instalment *i.e.* upto 31st March, 2022.

In the Books of Gomti Ltd.

Dr. 8% DEBENTURES ACCOUNT Cr.

Date	*Particulars*	₹	*Date*	*Particulars*	₹
2020			2019		
Mar. 31	To Debentureholders' A/c	2,00,000	April 1	By Balance b/d	6,00,000
Mar. 31	To Balance c/d	4,00,000			
		6,00,000			6,00,000
2021			2020		
Mar. 31	To Debentureholders' A/c	2,00,000	April 1	By Balance b/d	4,00,000
Mar. 31	To Balance c/d	2,00,000			
		4,00,000			4,00,000
2022			2021		
Mar. 31	To Debentureholders' A/c	2,00,000	April 1	By Balance b/d	2,00,000
		2,00,000			2,00,000

Dr. DEBENTUREHOLDERS' ACCOUNT Cr.

Date	*Particulars*	₹	*Date*	*Particulars*	₹
2020			2020		
Mar. 31	To Bank A/c	2,10,000	Mar. 31	By 8% Debentures A/c	2,00,000
			Mar. 31	By Premium on Redemption of Debentures A/c	10,000
		2,10,000			2,10,000
2021			2021		
Mar. 31	To Bank A/c	2,10,000	Mar. 31	By 8% Debentures A/c	2,00,000
			Mar. 31	By Premium on Redemption of Debentures A/c	10,000
		2,10,000			2,10,000

2022			2022		
Mar. 31	To Bank A/c	2,10,000	Mar. 31	By 8% Debentures A/c	2,00,000
			Mar. 31	By Premium on Redemption of Debentures A/c	10,000
		2,10,000			2,10,000

Dr. DEBENTURE REDEMPTION RESERVE ACCOUNT Cr.

Date	*Particulars*	₹	*Date*	*Particulars*	₹
2019			2019		
Mar. 31	To Balance c/d	60,000	Mar. 31	By Surplus in Statement of P & L	60,000
2020			2019		
Mar. 31	To General Reserve A/c	20,000	April 1	By Balance b/d	60,000
Mar. 31	To Balance c/d	40,000			
		60,000			60,000
2021			2020		
Mar. 31	To General Reserve A/c	20,000	April 1	By Balance b/d	40,000
Mar. 31	To Balance c/d	20,000			
		40,000			40,000
2022			2021		
Mar. 31	To General Reserve A/c	20,000	April 1	By Balance b/d	20,000
		20,000			20,000

Dr. DEBENTURE REDEMPTION INVESTMENT ACCOUNT Cr.

Date	*Particulars*	₹	*Date*	*Particulars*	₹
2019			2020		
Apr. 30	To Bank A/c	30,000	Mar. 31	By Balance c/d	30,000
		30,000			30,000
2020			2021		
Apr. 1	To Balance b/d	30,000	Mar. 31	By Balance c/d	30,000
		30,000			30,000
2021			2022		
Apr. 1	To Balance b/d	30,000	Mar. 31	By Bank A/c	30,000
		30,000			30,000

ILLUSTRATION 14.

Pragati Enterprises Ltd. (an unlisted company) issued 35,000, 6½% debentures of ₹100 each on October 1, 2011 redeemable as follows :

On 31st March 2015	5,000 Debentures

On 31st March 2016	5,000 Debentures
On 31st March 2017	7,000 Debentures
On 31st March 2018	7,000 Debentures
On 31st March 2019	11,000 Debentures

The Board decides to transfer to Debenture Redemption Reserve ₹20,000 and ₹1,60,000 on March 31, 2012 and 2013 respectively and balance required to be transferred to Debenture Redemption Reserve on March 31, 2014. Record necessary journal entries. Ignore entries for payment of interest. Investment as required by law was made in fixed deposit of the bank.

SOLUTION Books of Pragati Enterprise Ltd.

JOURNAL

Date	*Particulars*		*L.F.*	*Dr.* (₹)	*Cr.* (₹)
2011 Oct. 1	Bank A/c To 6½ % Debenture Application & Allotment A/c (Receipt of application money)	Dr.		35,00,000	 35,00,000
Oct. 1	6½ % Debenture Application & Allotment A/c To 6½ % Debentures A/c (Transfer of application money)	Dr.		35,00,000	 35,00,000
2012 March 31	Surplus in Statement of Profit and Loss To Debenture Redemption Reserve A/c (Transfer of profits to DRR)	Dr.		20,000	 20,000
2013 March 31	Surplus in Statement of Profit and Loss To Debenture Redemption Reserve A/c (Transfer of profits to DRR)	Dr.		1,60,000	 1,60,000
2014 March 31	Surplus in Statement of Profit and Loss To Debenture Redemption Reserve A/c (Transfer of profits to DRR : 10% of 35,00,000 = 3,50,000 *Less* : On 31.3.2012 20,000 On 31.3.2013 1,60,000 1,80,000 1,70,000)	Dr.		1,70,000	 1,70,000
April 30	Debenture Redemption Investment A/c To Bank A/c (Investment made equal to 15% of first instalment of ₹5,00,000)	Dr.		75,000	 75,000
2015 March 31	6½ % Debentures A/c To Debentureholders A/c (Amount due on redemption)	Dr.		5,00,000	 5,00,000

March 31	Debentureholders A/c	Dr.	5,00,000	
	To Bank A/c			5,00,000
	(Payment of amount due to Debentureholders)			
March 31	Debenture Redemption Reserve A/c	Dr.	50,000	
	To General Reserve A/c (Note 1)			50,000
	(Transfer of proportionate amount of DRR to General Reserve)			
2016				
March 31	6½ % Debentures A/c	Dr.	5,00,000	
	To Debentureholders A/c			5,00,000
	(Amount due on redemption)			
March 31	Debentureholders A/c	Dr.	5,00,000	
	To Bank A/c			5,00,000
	(Payment of amount due to Debentureholders)			
March 31	Debenture Redemption Reserve A/c	Dr.	50,000	
	To General Reserve A/c (Note 1)			50,000
	(Transfer of proportionate amount of DRR to General Reserve)			
April 30	Debenture Redemption Investment A/c	Dr.	30,000	
	To Bank A/c			30,000
	(Investment made equal to 15% of additional amount of ₹2,00,000 *i.e.,* ₹7,00,000 – ₹5,00,000)			
2017				
March 31	6½ % Debentures A/c	Dr.	7,00,000	
	To Debentureholders A/c			7,00,000
	(Amount due on redemption)			
March 31	Debentureholders A/c	Dr.	7,00,000	
	To Bank A/c			7,00,000
	(Payment of amount due to Debentureholders)			
March 31	Debenture Redemption Reserve A/c	Dr.	70,000	
	To General Reserve A/c (Note 1)			70,000
	(Transfer of proportionate amount of DRR to General Reserve)			
2018				
March 31	6½ % Debentures A/c	Dr.	7,00,000	
	To Debentureholders A/c			7,00,000
	(Amount due on redemption)			
March 31	Debentureholders A/c	Dr.	7,00,000	
	To Bank A/c			7,00,000
	(Payment of amount due to Debentureholders)			
March 31	Debenture Redemption Reserve A/c	Dr.	70,000	
	To General Reserve A/c (Note 1)			70,000
	(Transfer of proportionate amount of DRR to General Reserve)			

April 30	Debenture Redemption Investment A/c To Bank A/c (Investment made equal to 15% of additional amount of ₹4,00,000 *i.e.*, ₹11,00,000 – ₹7,00,000)	Dr.	60,000	60,000
2019 March 31	Bank A/c To Debenture Redemption Investment A/c (Investments amounting to ₹75,000 plus ₹30,000 plus ₹60,000 encashed before redemption of last instalment)	Dr.	1,65,000	1,65,000
March 31	6½% Debentures A/c To Debentureholders A/c (Amount due on redemption)	Dr.	11,00,000	11,00,000
March 31	Debentureholders A/c To Bank A/c (Payment of amount due to Debentureholders)	Dr	11,00,000	11,00,000
March 31	Debenture Redemption Reserve A/c To General Reserve A/c (Transfer of proportionate amount of DRR to General Reserve)	Dr.	1,10,000	1,10,000

Working Note

(1) DRR will be transferred to General Reserve A/c as follows :

On 31st March 2015 : $3{,}50{,}000 \times \frac{5{,}00{,}000}{35{,}00{,}000}$ = ₹ 50,000

On 31st March 2016 : $3{,}50{,}000 \times \frac{5{,}00{,}000}{35{,}00{,}000}$ = ₹ 50,000

On 31st March 2017 : $3{,}50{,}000 \times \frac{7{,}00{,}000}{35{,}00{,}000}$ = ₹ 70,000

On 31st March 2018 : $3{,}50{,}000 \times \frac{7{,}00{,}000}{35{,}00{,}000}$ = ₹ 70,000

On 31st March 2019 : $3{,}50{,}000 \times \frac{11{,}00{,}000}{35{,}00{,}000}$ = ₹1,10,000

ILLUSTRATION [illegible]

Akanksha Enterprises Ltd. (an unlisted company) issued 12,000, 6% Debentures of ₹100 each on September 1, 2012 redeemable at a premium of 7% as under :

On March 31, 2018	4,000 Debentures
On March 31, 2019	3,000 Debentures
On March 31, 2020	5,000 Debentures

The Board of Directors has also decided to transfer the required amount to Debenture Redemption Reserve in four equal annual instalments starting with March 31, 2014. Record necessary journal entries. Ignore entries for interest. Investment as required by law was made in fixed deposit of the bank.

SOLUTION :

Books of Akanksha Enterprises Ltd.

JOURNAL

Date	Particulars	L.F.	Dr. (₹)	Cr. (₹)
2012 Sept. 1	Bank A/c Dr.		12,00,000	
	To 6% Debenture Application & Allotment A/c			12,00,000
	(Receipt of application money)			
Sept. 1	6% Debenture Application & Allotment A/c Dr.		12,00,000	
	Loss on Issue of Debentures A/c Dr.		84,000	
	To 6% Debentures A/c			12,00,000
	To Premium on Redemption of Debentures A/c			84,000
	(Transfer of application money)			
2014 March 31	Surplus in Statement of Profit and Loss Dr.		30,000	
	To Debenture Redemption Reserve A/c			30,000
	(Transfer of profit to DRR)			
2015 March 31	Surplus in Statement of Profit and Loss Dr.		30,000	
	To Debenture Redemption Reserve A/c			30,000
	(Transfer of profit to DRR)			
2016 March 31	Surplus in Statement of Profit and Loss Dr.		30,000	
	To Debenture Redemption Reserve A/c			30,000
	(Transfer of profit to DRR)			
2017 March 31	Surplus in Statement of Profit and Loss Dr.		30,000	
	To Debenture Redemption Reserve A/c			30,000
	(Transfer of profit to DRR)			
April 30	Debenture Redemption Investment A/c Dr.		60,000	
	To Bank A/c			60,000
	(Investment made equal to 15% of first instalment of ₹4,00,000)			
2018 March 31	Bank A/c Dr.		15,000	
	To Debenture Redemption Investment A/c			15,000
	(Investments encashed equal to 15% of ₹1,00,000 *i.e.*, ₹4,00,000 – ₹3,00,000)			
March 31	6% Debentures A/c Dr.		4,00,000	
	Premium on Redemption of Debentures A/c Dr.		28,000	
	To Debentureholders A/c			4,28,000
	(Amount due on redemption)			
March 31	Debentureholders A/c Dr.		4,28,000	
	To Bank A/c			4,28,000
	(Payment of amount due to debentureholders)			

March 31	Debenture Redemption Reserve A/c Dr. To General Reserve A/c (Note 1) (Transfer of proportionate amount of DRR to General Reserve)		40,000	 40,000
2019 March 31	6% Debentures A/c Dr. Premium on Redemption of Debentures A/c Dr. To Debentureholders A/c (Amount due on redemption)		3,00,000 21,000	 3,21,000
March 31	Debentureholders A/c Dr. To Bank A/c (Payment of amount due to debentureholders)		3,21,000	 3,21,000
March 31	Debenture Redemption Reserve A/c Dr. To General Reserve A/c (Note 1) (Transfer of proportionate amount of DRR to General Reserve)		30,000	 30,000
April 30	Debenture Redemption Investment A/c Dr. To Bank A/c (Investment made equal to 15% of additional amount of ₹2,00,000 *i..e,* ₹5,00,000 – ₹3,00,000)		30,000	 30,000
2020 March 31	Bank A/c Dr. To Debenture Redemption Investment A/c (Investments encashed before redemption of last instalment)		75,000	 75,000
March 31	6% Debentures A/c Dr. Premium on Redemption of Debentures A/c Dr. To Debentureholders A/c (Amount due on redemption)		5,00,000 35,000	 5,35,000
March 31	Debentureholders A/c Dr. To Bank A/c (Payment of amount due to debentureholders)		5,35,000	 5,35,000
March 31	Debenture Redemption Reserve A/c Dr. To General Reserve A/c (Transfer of proportionate amount of DRR to General Reserve)		50,000	 50,000

Working Note :

(1) DRR will be transferred to General Reserve as follows :

On 31st March 2018 : $1{,}20{,}000 \times \dfrac{4{,}00{,}000}{12{,}00{,}000} =$ ₹40,000

On 31st March 2019 : $1{,}20{,}000 \times \dfrac{3{,}00{,}000}{12{,}00{,}000} =$ ₹30,000

On 31st March 2020 : $1{,}20{,}000 \times \dfrac{5{,}00{,}000}{12{,}00{,}000} =$ ₹50,000

ILLUSTRATION 15 (B).

Faith and Belief Ltd. has total redeemable debentures of ₹5,00,000. It decides to redeem these debentures in two instalments of ₹3,00,000 and ₹2,00,000 on December 31st 2018 and March 31st 2020 respectively. Assuming that the Company has sufficient funds in Debenture Redemption Reserve Account, pass necessary journal entries for the year ending March 31st 2020. *(C.B.S.E. Sample Paper, 2020)*

SOLUTION :

Faith and Belief Ltd.
JOURNAL

Date	*Particulars*		*L.F.*	*Dr.* (₹)	*Cr.* (₹)
2019 April 30	Debenture Redemption Investment A/c	Dr.		30,000	
	To Bank A/c				30,000
	(Investments made @ 15% of ₹2,00,000)				
2020 March 31	Bank A/c	Dr.		30,000	
	To Debenture Redemption Investment A/c				30,000
	(Investments encashed)				
”	Debentures A/c	Dr.		2,00,000	
	To Debenture Holders A/c				2,00,000
	(Debentures due for redemption)				
”	Debenture Holders A/c	Dr.		2,00,000	
	To Bank A/c				2,00,000
	(Payment made to debenture holders)				
”	Debenture Redemption Reserve A/c	Dr.		20,000	
	To General Reserve A/c				20,000
	(Transfer of proportionate Debenture Redemption Reserve i.e. 10% of ₹2,00,000 to General Reserve)				

Note : As stated in the question, Faith and Belief Ltd. has sufficient funds in DRR. It means it is an unlisted company and has 10% of redeemable debentures of ₹2,00,000 *i.e.,* ₹20,000 in DRR which is now transferred to General Reserve.

ILLUSTRATION 16.

On 1st April, 2016, the following balances appeared in the books of Shikhar Ltd. *(an unlisted company)*

	₹
10% Debentures	14,00,000
Premium on Redemption of Debentures	1,40,000
Debenture Redemption Reserve	75,000

The debentures were to be redeemed at a premium of 10% in *two equal annual instalments* beginning from 31st March, 2018. To meet the requirements of the Companies Act, 2013, the company transferred the balance amount to Debenture Redemption Reserve on 31st March, 2017. On 30th April, 2017, it met the requirements of the Companies Act, 2013 regarding Debenture Redemption Investment and redeemed the debentures on the scheduled dates.

You are required to pass necessary journal entries to record the above transactions in the books of Shikhar Ltd. *(Ignore interest on Debentures).* *(I.S.C. 2020)*

SOLUTION:

SHIKHAR LTD.

JOURNAL

Date	*Particulars*	*L.F.*	*Dr. Amount*	*Cr. Amount*
2017			₹	₹
March 31	Surplus in Statement of Profit and Loss(1) Dr.		65,000	
	To Debenture Redemption Reserve A/c			65,000
	(Transfer of profit equal to 10% of the face value of debentures to DRR)			
April 30	Debenture Redemption Investment A/c Dr.		1,05,000	
	To Bank A/c			1,05,000
	(Investment made equal to 15% of first instalment of ₹7,00,000)			
2018				
March 31	10% Debentures A/c Dr.		7,00,000	
	Premium on Redemption of Debentures A/c Dr.		70,000	
	To Debentureholders A/c			7,70,000
	(Amount due on redemption)			
March 31	Debentureholders A/c Dr.		7,70,000	
	To Bank A/c			7,70,000
	(Payment of amount due to debentureholders)			
March 31	Debenture Redemption Reserve A/c Dr.		70,000	
	To General Reserve A/c			70,000
	(Transfer of proportionate amount of DRR to General Reserve)			
2019				
March 31	Bank A/c Dr.		1,05,000	
	To Debenture Redemption Investment A/c			1,05,000
	(Investments encashed)			
March 31	10% Debentures A/c Dr.		7,00,000	
	Premium on Redemption of Debentures A/c Dr.		70,000	
	To Debentureholders A/c			7,70,000
	(Amount due on redemption)			
March 31	Debentureholders A/c Dr.		7,70,000	
	To Bank A/c			7,70,000
	(Payment of amount due to debentureholders)			
March 31	Debenture Redemption Reserve A/c Dr.		70,000	
	To General Reserve A/c			70,000
	(Transfer of proportionate amount of DRR to General Reserve)			

Working Note : (1)

	₹
Total amount required for transfer to DRR 10% of ₹14,00,000	1,40,000
Less : Existing Balance	75,000
	65,000

(3) Redemption of debentures by the purchase of own debentures in the open market : According to the Companies Act, a Company can, if authorised by its articles of association, redeem its debentures by purchasing them in the open market. Open market means purchasing own debentures from the stock market. This procedure is usually adopted by the Company only when its debentures are quoted at a discount on the stock exchange.

Important Notes

(1) It is assumed that the Company has sufficient balance in Debenture Redemption Reserve before initiating the purchase of debentures for cancellation. Hence, unless otherwise stated, there is no need to create DRR in this method.

(2) Also assume that required investment @15% has been made. Hence, there is no need to make investment.

After purchasing the debentures from the open market, the Company may use either of the following two options :

(A) Company may immediately cancel the debentures so purchased. Debentures will be cancelled only after passing the resolution by Board of Directors to this effect.

Or

(B) Company may not cancel the debentures but may keep them alive with a view to issuing them in future. The debentures so kept alive shall be treated as an "investment in the own debentures" by the Company.

(A) When own debentures are purchased for Immediate Cancellation :

For example, if a Company purchased 500 of its own debentures of ₹100 each at ₹98 in the open market and immediately cancels them after purchase, the following entries will be passed :

Date	*Particulars*		*L.F.*	*Dr. (₹)*	*Cr. (₹)*
	Own Debentures A/c	Dr.		49,000	
	To Bank A/c				49,000
	(500 debentures of ₹100 each purchased in the open market at ₹98 per debenture)				
	Debentures A/c	Dr.		50,000	
	To Own Debentures A/c				49,000
	To Profit on Redemption of Debentures A/c (or Profit on Cancellation A/c)				1,000
	(Cancellation of own debentures)				

Profit on Redemption of Debentures is a Capital profit. It should be used to write off any amount of capital loss given in the question such as, discount on issue etc. the balance will be transferred to Capital Reserve. The entry will be :

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
	Profit on Redemption of Debentures A/c	Dr.		1,000	
	To Capital Loss (if any)				1,000
	To Capital Reserve A/c				

If the purchase price of the debentures is more than the face value, there will be a loss on the redemption of such debentures and the loss will be debited to "Loss on Redemption of Debentures A/c". Suppose, Debentures of the face value of ₹20,000 are purchased in the market at ₹21,000, the entry will be :

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
	Own Debentures A/c	Dr.		21,000	
	To Bank A/c				21,000
	Debentures A/c	Dr.		20,000	
	Loss on Redemption of Debentures A/c	Dr.		1,000	
	To Own Debentures A/c				21,000

"Loss on Redemption of Debentures A/c" is a capital loss and is therefore written off against capital profits or in the absence of capital profits is written off from Statement of Profit and Loss.

ILLUSTRATION 17

On 31st March, 2022, Z Ltd. purchased its own 2,000, 8% debentures of the face value of ₹2,00,000 from the open market at ₹92 for immediate cancellation. The expenses of purchase amounted to ₹4,000. Pass Journal entries.

SOLUTION

Books of Z Ltd.

JOURNAL

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
2022					
March 31	Own Debentures A/c	Dr.		1,88,000	
	To Bank A/c				1,88,000
	(Purchase of 2,000 own debentures @92 each plus ₹4,000 paid for expenses)				
March 31	8% Debentures A/c	Dr.		2,00,000	
	To Own Debentures A/c				1,88,000
	To Profit on Redemption of Own Debentures A/c				12,000
	(Cancellation of own debentures)				
March 31	Profit on Redemption of Own Debentures A/c	Dr.		12,000	
	To Capital Reserve A/c				12,000
	(Transfer of profit on redemption of debentures to Capital Reserve)				

Notes :

(1) In case of open market purchase of own debentures it is assumed that the company has sufficient balance in DRR and 15% amount has been invested before initiating the purchase of own debentures for cancellation.

(2) It has been assumed that the company must have invested the required amount.

ILLUSTRATION 18.

Zodiac Ltd. purchased from open market its own 5,000, 8% Debentures of ₹100 each @₹103 per debenture for immediate cancellation. Brokerage paid @ 0.4%. Pass Journal entries.

SOLUTION :

JOURNAL

Date	*Particulars*		*L.F.*	*Dr.* (₹)	*Cr.* (₹)
	Own Debentures A/c(1)	Dr.		5,17,060	
	To Bank A/c				5,17,060
	(Purchase of 5,000 own debentures @₹103)				
	8% Debentures A/c	Dr.		5,00,000	
	Loss on Cancellation of Own Debentures A/c	Dr.		17,060	
	To Own Debentures A/c				5,17,060
	(Own debentures cancelled)				
	Statement of Profit & Loss	Dr.		17,060	
	To Loss on Cancellation of Own Debentures A/c				17,060
	(Loss on cancellation written off)				

Notes : 1. Amount paid for purchase of own debentures :

	₹
5,000 × ₹103	5,15,000
Add : Brokerage : 0.4% on ₹5,15,000	2,060
	5,17,060

2. Loss on cancellation will be written off against capital profits or in its absence from Statement of Profit & Loss.

ILLUSTRATION 19.

On 31st March, 2018, Vipul Ltd. had ₹30,00,000, 8% Debentures of ₹100 each outstanding.

On 1st June, 2018, it purchased in the open market, 20,000 of its own debentures @ ₹102 per debenture and cancelled these debentures immediately.

On 31st December, 2018, the remaining debentures were purchased @ ₹98 per debenture for immediate cancellation.

You are required to pass necessary journal entries for the redemption of debentures. (Ignore interest on debentures and entries for provisions regarding Debenture Redemption Reserve and Debenture Redemption Investment).

(I.S.C. 2019)

SOLUTION : JOURNAL OF VIPUL LTD.

Date	*Particulars*		*L.F.*	*Dr.* (₹)	*Cr.* (₹)
	Own Debentures A/c	Dr.		20,40,000	
	To Bank A/c				20,40,000
	(20,000 own debentures purchased @ ₹102)				
	8% Debentures A/c	Dr.		20,00,000	
	Loss on Cancellation of Own Debentures A/c	Dr.		40,000	
	To Own Debentures A/c				20,40,000
	(Own debentures cancelled at a loss)				
	Own Debentures A/c	Dr.		9,80,000	
	To Bank A/c				9,80,000
	(10,000 own debentures purchased @ ₹98)				
	8% Debentures A/c	Dr.		10,00,000	
	To Own Debentures A/c				9,80,000
	To Profit on Cancellation of Own Debentures A/c				20,000
	(Own debentures cancelled at a profit)				
	Profit on Cancellation of Own Debentures A/c	Dr.		20,000	
	Statement of Profit & Loss	Dr.		20,000	
	To Loss on Cancellation of Own Debentures A/c				40,000
	(Loss on cancellation written off)				

When own debentures are purchased for immediate cancellation and such debentures are redeemable at a premium :

When debentures redeemable at a premium are purchased as own debentures for immediate cancellation, premium payable on redemption will not be paid and hence it becomes a capital profit for the company.

While passing journal entry for cancellation of own debentures, Premium on Redemption of Debentures A/c should be debited.

ILLUSTRATION 20.

X Ltd. purchased its own 1,000; 7% Debentures of ₹100 each @₹97 per debenture. These debentures were redeemable @5% premium.

Pass necessary Journal entries for purchase and cancellation of debentures.

SOLUTION : JOURNAL

Date	*Particulars*		*L.F.*	*Dr.* (₹)	*Cr.* (₹)
	Own Debentures A/c	Dr.		97,000	
	To Bank A/c				97,000
	(Purchase of 1,000 Debentures of ₹100 each at ₹97 per debenture)				

Date	Particulars	L.F.	Dr. (₹)	Cr. (₹)
	7% Debentures A/c Dr.		1,00,000	
	Premium on Redemption of Debentures A/c Dr.		5,000	
	To Own Debentures A/c			97,000
	To Profit on Cancellation of Own Debenturs A/c			8,000
	(1,000 Debentures of ₹100 each cancelled)			
	Profit on Cancellation of Own Debentures A/c Dr.		8,000	
	To Capital Reserve A/c			8,000
	(Profit on cancellation transferred to Capital Reserve)			

ILLUSTRATION 21.

Shobha Ltd. purchased from open market its own 3,000, 9% Debentures of ₹100 each @₹106 per debenture for immediate cancellation. These debentures were redeemable at 5% premium. Company has a balance of ₹10,000 in Capital Reserve.

Pass necessary Journal entries.

SOLUTION :

JOURNAL

Date	*Particulars*	*L.F.*	*Dr.* (₹)	*Cr.* (₹)
	Own Debentures A/c Dr.		3,18,000	
	To Bank A/c			3,18,000
	(Purchase of 3,000 Debentures of ₹100 each at ₹106 per debenture)			
	9% Debentures A/c Dr.		3,00,000	
	Premium on Redemption of Debentures A/c Dr.		15,000	
	Loss on Cancellation of Own Debentures A/c Dr.		3,000	
	To Own Debentures A/c			3,18,000
	(3,000 Debentures of ₹100 each redeemable at ₹105 cancelled)			
	Capital Reserve A/c Dr.		3,000	
	To Loss on Cancellation of Own Debentures A/c			3,000
	(Loss on cancellation written off from Capital Reserve)			

Notes : Loss on Cancellation of Own Debentures is a capital loss. It is set off against Capital Reserve, if it has a balance.

ILLUSTRATION 22.

Guru Ltd. purchased its own 2,000, 8% Debentures of ₹100 each at ₹107 each from open market for immediate cancellation. These debentures were redeemable at 4% premium. Balance in Capital Reserve is ₹5,000.

Pass necessary Journal entries.

SOLUTION :

JOURNAL

Date	*Particulars*		*L.F.*	*Dr. (₹)*	*Cr. (₹)*
	Own Debentures A/c	Dr.		2,14,000	
	To Bank A/c				2,14,000
	(2,000 Own Debentures purchased @₹107 per debenture)				
	8% Debentures A/c	Dr.		2,00,000	
	Premium on Redemption of Debentures A/c	Dr.		8,000	
	Loss on Cancellation Own Debentures A/c	Dr.		6,000	
	To Own Debentures A/c				2,14,000
	(2,000 Own Debentures of ₹100 each redeemable @4% premium cancelled)				
	Capital Reserve A/c	Dr.		5,000	
	Statement of Profit & Loss	Dr.		1,000	
	To Loss on Cancellation of Own Debentures A/c				6,000
	(Loss on cancellation written off)				

Note : Loss on cancellation is set off against Capital Reserve upto the extent of the balance of Capital Reserve and the remaining amount from Statement of Profit & Loss.

ILLUSTRATION 23.

On 1st April, 2020, a company issued 4,000; 9% Debentures of ₹100 each at a discount of 10%, repayable at a premium of 10%. The terms of issue provided for the redemption of ₹40,000 debentures every year commencing from 31st March, 2022, either by purchase from open market or by draw of lots at the company's option.

On 31st March, 2022, the company purchased for cancellation its own debentures of the face value of ₹32,000 at ₹95 per debenture and ₹8,000 at ₹90 per debenture. The expenses of purchase amounted to ₹1,000. Record necessary Journal entries for redemption of 9% Debentures. Ignore entries relating to DRR and investment.

SOLUTION :

JOURNAL

Date	*Particulars*		*L.F.*	*Dr. (₹)*	*Cr. (₹)*
2022					
Mar. 31	Own Debentures A/c(1)	Dr.		38,600	
	To Bank A/c				38,600
	(Purchase of 400 own debentures of ₹100 each for immediate cancellation)				
	9% Debentures A/c	Dr.		40,000	
	Premium on Redemption of Debentures A/c	Dr.		4,000	
	To Own Debentures A/c				38,600
	To Profit on Cancellation of Own Debentures A/c				5,400
	(Cancellation of 400 own debentures)				

	Profit on Cancellation of Own Debentures A/c Dr. To Capital Reserve A/c (Transfer of profit on cancellation of own debentures to Capital Reserve)		5,400	5,400

Note : (1) Amount paid for purchase of own debentures :

	₹
320 debentures @₹95 each	30,400
80 debentures @₹90 each	7,200
	37,600
Add : Expenses of purchase	1,000
	38,600

ILLUSTRATION 24.

X Ltd. (an unlisted company) made an issue of 2,000, 15% debentures of ₹100 each. Of these, debentures of the face value of ₹50,000 are to be redeemed annually commencing from 2019-20, either by drawings at par or by purchase in the open market at the company's option.

The Company transferred the required amount to DRR on 31st March 2019 and invested the required amount on 30th April, 2019.

On 31st March, 2020, the company purchased for cancellation ₹40,000 debentures at ₹95 and ₹10,000 debentures at ₹98. The expenses of purchases amounted to ₹500.

Make necessary journal entries for the redemption of debentures.

SOLUTION :

X **Ltd.**

JOURNAL

Date	*Particulars*	*L.F.*	*Dr.* (₹)	*Cr.* (₹)
2019 March 31	Surplus *i.e.*, Balance in Statement of P & L Dr. To Debenture Redemption Reserve A/c (Transfer of 10% of issued amount of ₹2,00,000 to DRR)		20,000	20,000
April 30	Debenture Redemption Investment A/c Dr. To Bank A/c (Investment made @15% of ₹50,000 being the face value of debentures to be redeemed)		7,500	7,500
2020 March 31	Own Debentures A/c Dr. To Bank A/c⁽¹⁾ (Purchase of own debentures 400 @ 95 and 100 @ 98 plus ₹500 expenses for purchase)		48,300	48,300
March 31	15% Debentures A/c Dr. To Own Debentures A/c To Profit on Redemption of Debentures A/c (Cancellation of own debentures)		50,000	48,300 1,700

Date	Particulars		Dr. (₹)	Cr. (₹)
March 31	Profit on Redemption of Debentures A/c To Capital Reserve A/c (Transfer of profit on redemption to Capital Reserve A/c)	Dr.	1,700	1,700
March 31	Debenture Redemption Reserve A/c To General Reserve A/c (One-fourth amount of DRR transferred to General Reserve on redemption of one-fourth debentures)	Dr.	5,000	5,000

Notes :

(1) Amount paid for the purchase of debentures :

	₹
400 Debentures × ₹95 per Debenture	38,000
100 Debentures × ₹98 per Debenture	9,800
	47,800
Add : Expenses	500
Total Payment	48,300

(2) Company has decided to redeem debentures for ₹50,000 every year. Hence, investment for ₹7,500 will not be encashed every year. This amount will remain invested until the final redemption.

(3) Proportionate amount of DRR will be transferred to General Reserve.

ILLUSTRATION 25.

On 1st April, 2018, an unlisted Company made an issue of 1,000, 10% Debentures of ₹100 each. The terms of issue provided for the redemption of ₹10,000 Debentures annually, commencing from 31st March, 2020, either by drawing at par or by purchase in the market at the Company's option.

The Company transferred the required amount to DRR on 31st March 2019 and invested the required amount on 30th April, 2019.

On 31st March, 2020, the Company purchased for cancellation ₹4,000 of its debentures at 96; ₹3,000 at 98 and ₹1,000 at 98 $\frac{1}{2}$. The expenses of purchase amounted to ₹35.

Record the above transactions in the Company's Ledger for the year 2019-20 including interest on debentures.

SOLUTION :

Dr. DEBENTURE REDEMPTION INVESTMENT ACCOUNT Cr.

Date	Particulars	₹	Date	Particulars	₹
2019			2020		
Apr. 30	To Bank A/c[2]	1,500	Mar. 31	By Balance c/d	1,500

OWN DEBENTURES ACCOUNT

Dr. Cr.

Date	Particulars	₹	Date	Particulars	₹
2020 Mar. 31	To Bank A/c	7,800	2020 Mar. 31	By 10% Debentures A/c	7,800

10% DEBENTURES ACCOUNT

Dr. Cr.

Date	Particulars	₹	Date	Particulars	₹
2020 Mar. 31	To Own Debentures A/c ₹4,000 @ 96 3,840 ₹3,000 @ 98 2,940 ₹1,000 @ $98\frac{1}{2}$ 985 *Add :* Expenses 35	7,800	2019 April 1	By Balance b/d	1,00,000
Mar. 31	To Profit on Redemption A/c	200			
Mar. 31	To Debentureholders A/c (Shortfall met)	2,000			
Mar.31	To Balance c/d	90,000			
		1,00,000			1,00,000

PROFIT ON REDEMPTION ACCOUNT

Dr. Cr.

Date	Particulars	₹	Date	Particulars	₹
2020 Mar. 31	To Capital Reserve A/c	200	2020 Mar. 31	By 10% Debentures A/c	200

INTEREST ON DEBENTURES ACCOUNT

Dr. Cr.

Date	Particulars	₹	Date	Particulars	₹
2020 Mar. 31	To Debentureholder's A/c	10,000	2020 Mar. 31	By Statement of P & L (Transfer)	10,000

DEBENTURE REDEMPTION RESERVE ACCOUNT

Dr. Cr.

Date	Particulars	₹	Date	Particulars	₹
2020 Mar. 31	To General Reserve A/c(1)	1,000	2019 April 1	By Balance b/d (10% of ₹1,00,000)	10,000
Mar. 31	To Balance c/d	9,000			
		10,000			10,000

Working Notes :

(1) Out of total debentures of ₹1,00,000, debentures amounting to ₹10,000 have been redeemed. Hence, $\frac{1}{10}$th of DRR has been transferred to General Reserve.

(2) Investment is made equal to 15% of annual redemption of ₹10,000.

ILLUSTRATION 26.

On 1st April, 2018, an unlisted company made an issue of ₹2,00,000, 6% Debentures of ₹100 each, repayable at a premium of 10%. The terms of issue provided for the redemption of 400 debentures every year starting from 31-3-2018 either by purchase from the open market or by draw of lots at the company's option.

On 31-3-2020, the company purchased for cancellation 300 Debentures at 95% and 100 Debentures at 90%. Required amount was transferred to DRR and investment was made as per law.

Pass the necessary Journal entries for the issue and redemption of debentures.

SOLUTION :

JOURNAL

Date	*Particulars*		*L.F.*	*Dr.* (₹)	*Cr.* (₹)
2018					
April 1	Bank A/c	Dr.		2,00,000	
	To 6% Debentures Application & Allotment A/c				2,00,000
	(Application money received on 2,000, 6% debentures of ₹100 each)				
April 1	6% Debentures Application & Allotment A/c	Dr.		2,00,000	
	Loss on Issue of Debentures A/c	Dr.		20,000	
	To 6% Debentures A/c				2,00,000
	To Premium on Redemption of Debentures A/c				20,000
	(Transfer of application money)				
2019					
March 31	Statement of Profit & Loss	Dr.		20,000	
	To Loss on Issue of Debentures A/c				20,000
	(Loss on issue of debentures written off)				
March 31	Surplus *i.e.*, Balance in Statement of Profit & Loss	Dr.		20,000	
	To Debenture Redemption Reserve A/c				20,000
	(DRR created equal to 10% of ₹2,00,000)				
April 30	Debenture Redemption Investment A/c	Dr.		6,000	
	To Bank A/c				6,000
	(Investment made @15% of the face value of debentures to be redeemed)				
2020					
March 31	Own Debentures A/c(1)	Dr.		37,500	
	To Bank A/c				37,500
	(Own debentures purchased)				
March 31	6% Debentures A/c	Dr.		40,000	
	To Own Debentures A/c				37,500
	To Profit on Cancellation of Debentures A/c				2,500
	(Cancellation of own debentures)				

March 31	Profit on Cancellation of Debentures A/c	Dr.		2,500	
	Premium on Redemption of Debentures A/c(2)	Dr.		4,000	
	To Capital Reserve A/c				6,500
	(Profit on redemption of debentures transferred to Capital Reserve)				
March 31	Debenture Redemption Reserve A/c	Dr.		4,000	
	To General Reserve A/c				4,000
	(Amount proprotionate to ₹40,000 debentures redeemed transferred to General Reserve)				

Working Notes :

(1) Amount paid for purchase of own debentures :

	₹
300 Debentures × ₹95 per Debenture	28,500
100 Debentures × ₹90 per Debenture	9,000
	37,500

(2) Since 400 debentures have been redeemed by purchase in the open market, 10% premium payable on redemption of these debentures will not be paid and hence it becomes a capital profit and is transferred to Capital Reserve.

(II) When own debentures are kept as 'Investment' It is not necessary for a Company to immediately cancel its own debentures after purchasing them. In fact, when a Company has surplus funds, instead of investing these funds in the securities of other Companies, it buys its own debentures as investment. This is due to the following reasons :

I. Sometimes, the own debentures are available in the open market at less than the face value.

II. It would be saving the interest which would otherwise have been payable on such debentures.

III. Such debentures are kept alive and can again be sold off in the market.

When a Company purchases its **own debentures** as investment and not for cancellation, an account named, **"Investment in Own Debentures Account"** is debited instead of **"Own Debentures Account"**. For example, if a Company purchased ₹50,000 of its own debentures at ₹49,000 as investment, the entry will be :

Date	*Particulars*		*L.F.*	*Dr.* (₹)	*Cr.* (₹)
	Investment in Own Debentures A/c	Dr.		49,000	
	To Bank A/c				49,000

It should be noted that in the above entry **"Investments in Own Debentures A/c"** will be debited with the amount actually paid, disregarding the face value of debentures purchased. Profit or Loss on the purchase is not recorded in the above entry, because own debentures in this case have been purchased as an asset and no profit or loss arises on the purchase of an asset. **Investment in own debentures** will appear on the assets side of the Company's balance sheet at purchase price, *i.e.*, ₹49,000. If the above company had issued 15% debentures of the total amount of ₹5,00,000, these will appear in the balance sheet as follows :

BALANCE SHEET

as at ....

Particulars	*Note No.*	*Current Year*	*Previous Year*
		₹	₹
I. EQUITY AND LIABILITIES :			
Non-Current Liabilities :			
Long term Borrowings	1	5,00,000	
II. ASSETS :			
Non Current Assets :			
Non-Current Investments*	2	49,000	

Notes to Accounts :

(1) **Long term Borrowings :**	₹
15% Debentures	5,00,000
(2) **Non-Current Investments :**	
Own Debentures (Face Value ₹50,000)	49,000

*Own Debentures will be shown in the Balance Sheet as Current or Non Current Investments depending on the time of cancellation.

ILLUSTRATION 27.

An unlisted Company had ₹5,00,000, 15% Debentures outstanding on 1st April, 2020. On the same date, as per the terms of issue, the company purchased ₹50,000 debentures at 98 in the open market.

Give journal entries, if (1) the debentures are purchased for immediate cancellation, (2) if the debentures are purchased as investment.

Also show how the above debentures will be shown in the Company's Balance Sheet in both the cases. Ignore entries relating to DRR and investing the 15% amount.

SOLUTION :

(1) If debentures are purchased for immediate cancellation :

JOURNAL

Date	*Particulars*		*L.F.*	*Dr. (₹)*	*Cr. (₹)*
2020					
April 1	Own Debentures A/c	Dr.		49,000	
	To Bank A/c				49,000
	(₹50,000 debentures purchased at 98% for immediate cancellation)				
April 1	15% Debentures A/c	Dr.		50,000	
	To Own Debentures A/c				49,000
	To Profit on Redemption of Debentures A/c				1,000
	(Cancellation of own Debentures)				

April 1	Profit on Redemption of Debentures A/c Dr. To Capital Reserve A/c (Profit on redemption transferred to Capital Reserve A/c)		1,000	1,00

BALANCE SHEET
as at 31st March, 2021

Particulars	*Note No.*	*31st March 2021*	*31st March 2020*
		₹	₹
I. EQUITY AND LIABILITIES :			
Non Current Liabilities :			
Long-term Borrowings	1	4,50,000	5,00,000

Notes to Accounts :

	₹
(1) **Long-term Borrowings :**	
15% Debentures	4,50,000

(2) If debentures are purchased as investments :

JOURNAL

Date	*Particulars*	L.F.	Dr. (₹)	Cr. (₹)
2020 April 1	Investment in Own Debentures A/c Dr. To Bank A/c (₹50,000 own debentures purchased as investment at 98%)		49,000	49,000

BALANCE SHEET
as at 31st March, 2021

Particulars	*Note No.*	*31st March 2021*	*31st March 2020*
		₹	₹
I. EQUITY AND LIABILITIES :			
Non-Current Liabilities :			
Long term Borrowings	1	5,00,000	5,00,000
II. ASSETS :			
Non Current Assets :			
Non-Current Investments*	2	49,000	

Notes to Accounts :

	₹
(1) **Long term Borrowings :**	
15% Debentures	5,00,000

(2) **Non-Current Investments :** Own Debentures (Face Value ₹50,000)	49,000

*Own Debentures will be shown in the Balance Sheet as Current or Non Current Investments depending on the time of cancellation.

Debentures purchased as investment may be sold by the Company in the open market or may be cancelled, whenever it so decides. If in the above illustration, the Company wants to cancel its 'investment in own debentures' the following entry will be passed for their cancellation :

JOURNAL

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
2020					
April 1	15% Debentures A/c	Dr.		50,000	
	To Investment in Own Debentures A/c				49,000
	To Profit on Redemption A/c				1,000
April 1	Profit on Redemption A/c	Dr.		1,000	
	To Capital Reserve A/c				1,000

Profit or Loss on Resale of Own Debentures :

Such profit or loss is treated as revenue profit or loss and hence it is transferred to Statement of Profit and Loss.

Notes :	(*i*)	Profit on sale of 'Investment in own debentures' is shown under **Other Income** in the Statement of Profit and Loss.
	(*ii*)	Loss on sale of 'Investment in own debentures' is shown under **Other Expenses** in the Statement of Profit and Loss.

ILLUSTRATION 28.

(Purchase of Own Debentures as Investment)

Gunjan Constructions Ltd. (an unlisted Company) issued 5,000, 8% debentures of ₹500 each. The Board of directors decided to purchase 1,000 debentures at a price of ₹485 each for investment purpose. After few months, they decided to sell off these debentures @ ₹510 each in the market. Record necessary entries to show above transactions.

SOLUTION :

Gunjan Constructions Ltd.

JOURNAL

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
On the date of issue	Bank A/c	Dr.		25,00,000	
	To Debenture Application & Allotment A/c				25,00,000
	(Debenture application money received)				
On the date of issue	Debenture Application & Allotment A/c	Dr.		25,00,000	
	To 8 % Debentures A/c				25,00,000
	(Application money transferred to Debentures Account)				

On the date of purchase	Investments in Own Debentures A/c Dr.		4,85,000	
	To Bank A/c			4,85,000
	(Purchase of 1,000 debentures of ₹500 each at ₹485 each as investments)			
On the date of sale	Bank A/c Dr.		5,10,000	
	To Investments in Own Debentures A/c			4,85,000
	To Profit on Sale of Investments A/c			25,000
	(Investments in own debentures sold at ₹510 each)			
On the date of sale	Profit on Sale of Investments A/c Dr.		25,000	
	To Statement of Profit and Loss			25,000
	(Profit on sale of investments transferred to Statement of Profit and Loss)			

Note : The Company is not required to create DRR and also there is no need to invest the 15% amount because the debentures are purchased for investment and not for cancellation.

ILLUSTRATION 29.

On 1-7-2020, Paushak Ltd. purchased its 800, 10% debentures of ₹500 each at ₹480 each for investment purposes. Brokerage paid 0.5%. On 1-11-2020, it sold 600 debentures at ₹492 each. Brokerage paid 0.5%. On 31-3-2021, it decided to cancel the remaining debentures.

Journalise the transactions in the books of Paushak Ltd.

SOLUTION :

Paushak Ltd.

JOURNAL

Date	*Particulars*	*L.F.*	*Dr. (₹)*	*Cr. (₹)*
2020				
July 1	Investment in Own Debentures A/c(2) Dr.		3,85,920	
	To Bank A/c			3,85,920
	(Purchase of 800 own debentures as investment @₹480 each plus brokerage @0.5%)			
Nov. 1	Bank A/c(3) Dr.		2,93,724	
	To Investment in Own Debentures A/c			2,89,440
	To Profit on Sale of Investments A/c			4,284
	(Sale of 600 own debentures @₹492 each less brokerage @0.5%)			
Nov. 1	Profit on Sale of Investments A/c Dr.		4,284	
	To Statement of Profit & Loss			4,284
	(Profit on sale of 600 own debentures transferred to Statement of P & L)			
2021				
March 31	10% Debentures A/c Dr.		1,00,000	
	To Investment in Own Debentures A/c(4)			96,480
	To Profit on Cancellation of Debentures A/c			3,520
	(200 own debentures cancelled)			

March 31	Profit on Cancellation of Debentures A/c	Dr.	3,520	
	To Capital Reserve A/c			3,520
	(Profit on cancellation transferred to Capital Reserve)			

Working Notes :

(1) It is assumed that the Company has adequate balance in DRR.

(2) Cost of Own Debentures purchased :

800 × ₹480	3,84,000
Add : Brokerage : 3,84,000 × 0.5%	1,920
	3,85,920

(3) Sale Price of 600 Own Debentures :

600 × ₹492	2,95,200	
Less : Brokerage : 2,95,200 × 0.5%	1,476	2,93,724
Less : Cost of 600 Own Debentures : $3,85,920 \times \frac{600}{800}$		2,89,440
Profit on Sale of own debentures		4,284

(4) Cost of 200 Own Debentures :

$$3,85,920 \times \frac{200}{800} = ₹96,480$$

Interest on Own Debentures

When a Company purchases its own debentures from the open market and instead of immediately cancelling these debentures the debentures are carried as an investment, interest saved on such debentures must be reckoned as income. For example, if a Company had issued ₹5,00,000, 10% Debentures and out of these it purchases ₹1,00,000 Debentures itself and carries the same as investment, the entries for interest will be :—

		₹	₹
Interest on Debentures A/c	Dr.	50,000	
To Debentureholders A/c			40,000
To Interest on Own Debentures A/c			10,000
(Interest due on ₹4,00,000 debentures credited to debentureholders and on ₹1,00,000 debentures to Interest on own debentures account)			
Debentureholders A/c	Dr.	40,000	
To Bank A/c			40,000
(Interest paid to debentureholders)			
Interest on Own Debentures A/c	Dr.	10,000	
To Statement of Profit and Loss			10,000
(Interest on own debentures transferred to Statement of Profit and Loss)			

	Statement of Profit and Loss Dr. To Interest on Debentures A/c (Transfer of debenture interest to Statement of Profit and Loss)		50,000	50,000

The total amount of interest *i.e.*, ₹40,000 + ₹10,000 = ₹50,000 is shown as 'Finance Costs' in the Statement of P & L and the portion of interest pertaining to investment in own debentures *i.e.* ₹10,000 is treated as income and shown as 'Other Income' in the Statement of P & L.

ILLUSTRATION 32.

On 1st April, 2020, *X* Ltd. had 20,000, 9% Debentures of ₹100 each. On 1st October, 2020, the company purchased from the open market 5,000 debentures @ ₹96 each as investment. Debentures interest is payable on 30th September and 31st March. On 31st March, 2021, the company cancelled all the debentures purchased on 1st October, 2020. Pass necessary Journal entries in the books of the company.

SOLUTION :

X Ltd.
JOURNAL

Date	*Particulars*	*L.F.*	*Dr. (₹)*	*Cr. (₹)*
2020 Sept. 30	Debenture Interest A/c Dr. To Debentureholder's A/c (Interest due on debentures @ 9% p.a. for six months ended 30th September, 2020)		90,000	90,000
Sept. 30	Debentureholder's A/c Dr. To Bank A/c (Interest paid on debentures)		90,000	90,000
Oct. 1	Investment in Own Debentures A/c Dr. To Bank A/c (Purchase of 5,000 own debentures @ ₹96 each as investment)		4,80,000	4,80,000
2021 March 31	Debenture Interest A/c Dr. To Debentureholders' A/c To Interest on Own Debentures A/c (Interest on 15,000 outside debentures for six months and interest on 5,000 own debentures)		90,000	67,500 22,500
March 31	Debentureholders' A/c Dr. To Bank A/c (Interest paid to outside debentureholders)		67,500	67,500
March 31	9% Debentures A/c Dr. To Investment in Own Debentures A/c To Profit on Cancellation of Debentures A/c (Cancellation of 5,000 own debentures)		5,00,000	4,80,000 20,000

March 31	Profit on Cancellation of Debentures A/c Dr. To Capital Reserve A/c (Profit on cancellation of debentures transferred to Capital Reserve)		20,000	20,000
March 31	Interest on Own Debentures A/c Dr. To Statement of Profit and Loss (Interest on own debentures transferred to Statement of Profit and Loss)		22,500	22,500
March 31	Statement of Profit and Loss Dr. To Debenture Interest A/c (Debenture interest transferred to Statement of Profit and Loss)		1,80,000	1,80,000

Working Note : It is assumed that the Company has sufficient balance in D.R.R.

SHORT ANSWER QUESTIONS

Q. 1. What is meant by Redemption of Debentures?

Ans. Redemption of debentures means repayment of the amount of debentures to debentureholders. In other words, redemption refers to discharge of liability on account of debentures by repaying the due amount of debentures.

Q. 2. Name two sources of finance for redemption of debentures.

Ans. (*i*) Redemption out of capital.

(*ii*) Redemption out of profits.

Q. 3. What is meant by redemption of debentures out of Capital?

Ans. When no profits are set aside for redemption of debentures it is called redemption out of Capital. In such a case no profits are transferred to Debenture Redemption Reserve.

Q. 4. What is meant by redemption of debentures out of Profits?

Ans. When profits equal to the amount utilised for repayment to debentureholders is transferred from Surplus of Statement of Profit and Loss to a newly opened account titled 'Debenture Redemption Reserve Account' it is called redemption out of profits.

Q. 5. Mention, in brief, SEBI Guideline regarding Debenture Redemption Reserve.

Ans. As per SEBI Guidelines, a listed company is not required to create any DRR whereas an unlisted company shall create DRR equivalent to at least 10% of the amount of debentures outstanding **before starting the redemption of debentures.**

Q.6. Which Companies are exempted from creating 'Debenture Redemption Reserve' by the SEBI?

Ans. (*i*) Debentures issued by All India Financial Institutions regulated by RBI;

(*ii*) Banking Companies;

(*iii*) Non Banking Finance Companies registered with RBI;

(*iv*) Housing Finance Companies registered with National Housing Bank; and

(*v*) Other Listed Companies.

Q. 7. Profit on redemption of debentures is transferred to which account?

Ans. Capital Reserve Account.

Q. 8. What is meant by redemption of debentures by lump sum payment?

Ans. Under this method, the Company redeems whole of its debentures in one lump-sum at the expiry of a specified period, *i.e.*, at maturity date of the debentures or earlier at the option of the company.

Q. 9. What is meant by redemption of debentures by purchase of own debentures in the open market?

Ans. When a company purchases its own debentures through stock exchange for the purpose of cancellation, such an act of purchasing and cancelling the debentures constitutes redemption by purchase in the open market.

Q. 10. How would you treat the profit on cancellation of own debentures purchased by the Company in the Open Market?

Ans. It is a Capital profit. It should be used to write off any amount of capital loss given in the question such as discount on issue, etc. and the balance will be transferred to Capital Reserve.

Q. 11. Give an advantage of Redemption of debentures by purchase in the open market.

Ans. Usually a Company purchases its own debentures when they are quoted below par. Hence, the Company earns profit on redemption equal to the amount required to redeem them and the amount paid in purchasing them.

Q. 12. *X* Ltd. **(an unlisted company)** wants to redeem 5,000, 5% Debentures of ₹100 each at 5% premium. How much amount it must transfer to Debenture Redemption Reserve, if it has already a balance of ₹40,000 in Debenture Redemption Reserve Account?

Ans. ₹10,000.

Q. 13. What is the balance of Debenture Redemption Reserve transferred to General Reserve? *(ISC Specimen Question Paper, 2018)*

Ans. The amount proportionate to the debentures redeemed shall be transferred from Debenture Redemption Reserve (DRR) to General Reserve. For example, if the amount of Outstanding Debentures is ₹10,00,000 and there is a DRR of ₹1,00,000, then if 40% *i.e.*, ₹4,00,000 debentures are redeemed, 40% of ₹1,00,000 *i.e.*, ₹40,000 shall be transferred to General Reserve.

Q. 14. State two reasons for a company to purchase its own debentures from the open market. *(I.S.C. 2018)*

Ans. The company may purchase its own debentures in the open market with the objective of :

(*i*) Immediate cancellation; and

(*ii*) Keeping them as investments (to be cancelled or reissued at a later date).

Q. 15. What is the maximum limit of debentures which companies, other than Banking Companies and All India Financial Institutions, can redeem out of capital? *(I.S.C. 2020)*

Ans. (*i*) Listed companies are not required to create any Debenture Redemption Reserve. Hence, they can redeem all the debentures out of capital.

(*ii*) Unlisted companies are required to create Debenture Redemption Reserve equal to atleast 10% of outstanding debentures out of divisible profits. Hence, they can redeem 90% of their debentures out of capital.

PRACTICAL QUESTIONS

(Q. No. 1 to 30 are strictly according to the serial order of illustrations)

Methods of Redemption of Debentures

Lump-sum Payment at the end of Fixed Period :

Q. 1. Kaveri Ltd. **(an unlisted company)** issued 50,000, 8% Debentures of ₹100 each at par on Oct. 1, 2015 redeemable on March, 31, 2020. It was decided to invest 15% of the face value of debentures to be redeemed towards Debenture Redemption Investment on 30th April, 2019. Debentures were redeemed on due date. Record necessary entries for issue and redemption of debentures.

[**Ans.** Debenture Redemption Reserve created for ₹5,00,000 on March 31, 2019. Debenture Redemption Investment made for ₹7,50,000 on 30th April, 2019.]

Q. 2. On 1st April, 2016, *F* Ltd. **(an unlisted company)** issued ₹40,00,000, 7% Debentures of ₹100 each at a premium of 5%, redeemable at a premium of 10% at the end of 4 years. Investment as required by law was made in fixed deposit of the bank on 30th April earning interest @ 6% p.a.

Pass journal entries at the time of Redemption of Debentures.

[**Ans.** Debenture Redemption Reserve created for ₹4,00,000 on 31st March, 2019. Debenture Redemption Investment ₹6,00,000 made on 30th April, 2019.]

Note : Interest on investment will be calculated for 11 months.

Q. 3. Bank of Baroda issued 8,000, 8% Debentures of ₹100 each at a premium of 6% on 1st April, 2013 redeemable on 31st March, 2022. Record necessary entries for issue and redemption of debentures.

[**Ans.** No Debenture Redemption Reserve and investment is required for Banking Companies.]

Q. 4. On 1st April 2016, Rathee Steel Ltd. **(a listed company)** issued 60,000, 7% Debentures of ₹50 each at par, redeemable at 6% premium after six years. Debentures were redeemed on due. Pass necessary entries for issue and redemption of debentures. It is the policy of the company to write off all capital losses in the first year itself.

[**Ans.** (*i*) No DRR will be created since Rathee Ltd. is a listed company.

(*ii*) Investment will be made @ 15% of ₹30,00,000, since listed Companies are also required to make the minimum investment of 15%.]

Q. 5. On 1st April, 2018, the following balances appeared in the books of Blue and Green Ltd. **(an unlisted company)** :

12% Debentures (Redeemable on 31st August, 2020)	₹20,00,000
Debenture Redemption Reserve	₹ 50,000

The company met the requirements of Companies Act, 2013 regarding Debenture Redemption Reserve and Debenture Redemption investments and redeemed the debentures.

Ignoring interest on investments, pass necessary Journal entries for the above transactions in the books of company.

[**Ans.** Amount transferred to DRR ₹1,50,000. Debenture Redemption Investment ₹3,00,000. DRR transferred to General Reserve ₹2,00,000.]

Q. 6. Gati Ltd. **(an unlisted company)** has issued 30,000, 8% Debentures of ₹100 each of which one-third is due for redemption on March 31st 2022. The company has in its Debenture Redemption Reserve Account a balance of ₹1,20,000 on 31st March, 2021. Required Investment is made in fixed deposit on 30th April 2021 bearing interest @6% p.a. Record the necessary journal entries for the Redemption of Debentures.

[**Ans.** Amount transferred to Debenture Redemption Reserve ₹1,80,000. Debenture Redemption Investment ₹1,50,000. Interest received on fixed deposit ₹8,250. DRR transferred to General Reserve ₹1,00,000.]

Hint : One-third of Debenture Redemption Reserve will be transferred to General Reserve A/c since one-third debentures are redeemed.

Q. 7. On April 1st, 2018 following were the balances of Blue Bird Ltd. **(an unlisted company)** :

10% Debentures (redeemable on 31st March, 2020)	₹30,00,000
Debenture Redemption Reserve	₹ 1,00,000

Required investment was made earning interest @ 8% p.a.

On 31 March, 2019 the Board of Directors transferred the required amount to DRR and debentures were redeemed.

Pass necessary Journal entries for the above transactions in the books of the company.

[**Ans.** ₹2,00,000 will be transferred from Surplus in Statement of P & L to Debenture Redemption Reserve A/c. Debenture Redemption Investment made for ₹4,50,000 on 30th April, 2019. Interest received ₹33,000.]

Q. 8. *X* Ltd., **(an unlisted company)** had issued ₹8,00,000, 9% debentures which are due to be redeemed **out of profits** on 1st Oct. 2019 at a premium of 5%. The company had a Debenture Redemption Reserve of ₹4,14,000. The Company invested the required amount in fixed deposit in a Bank on 30th April, 2019 earning interest at 10% p.a. Pass necessary journal entries for the redemption of debentures.

[**Ans.** Amount transferred to Debenture Redemption Reserve ₹3,86,000 on 31st March, 2019. Debenture Redemption Investment ₹1,20,000 on 30th April, 2019; Interest received for five months ₹5,000.]

Note : Since the debentures are to be redeemed fully out of profits, debenture redemption reserve will be created with an amount equal to 100% of debentures redeemed.

Q. 9. On 1-1-2015 an **unlisted Company** issued 15,000, 10% Debentures of ₹100 each at par which were repayable at a Premium of 15% on 31-3-2020. On the date of maturity, the company decided to redeem the above mentioned 10% Debentures as per the terms of issue, **out of profits.** Required investment is made on 30th April, 2019 in fixed deposit bearing interest @8% p.a. Bank deducted TDS @10% on its maturity *i.e.* 31st March 2020.

Pass the necessary journal entries in the books of the Company for the redemption of Debentures.

[**Ans.** Debenture Redemption Reserve Created for ₹15,00,000. Debenture Redemption Investment ₹2,25,000; Interest on Investment ₹16,500. TDS ₹1,650.]

Note : Since the debentures are to be redeemed fully out of profits, debenture redemption reserve will be created with the full amount of debentures redeemed.

Q. 10. *X* Ltd. **(an unlisted company)** issued ₹80,00,000, 8% debentures of ₹100 each on 1st April, 2012. The terms of issue stated that the debentures were to be redeemed at a premium of 5% on 30th June, 2020. The company decided to transfer out of profits ₹4,00,000 to Debenture Redemption Reserve on 31st March, 2019 and ₹4,00,000 on 31st March, 2020.

Pass the necessary Journal entries regarding the issue and redemption of debentures, without providing for either the interest or loss on issue of debentures.

[**Ans.** Debenture Redemption Investment ₹12,00,000; DRR transferred to General Reserve ₹8,00,000.]

Q. 11. Chandra Tubes Ltd. **(an unlisted company)** issued 70,000, 7% debentures of ₹100 each on June 30, 2016 redeemable at a premium of 6% on July 1, 2020. The Board of Directors have decided to transfer out of profits ₹2,50,000 to Debenture Redemption Reserve on March 31, 2018, ₹2,50,000 on March 31, 2019 and balance on March 31, 2020. Record necessary journal entries regarding issue and redemption of debentures. Ignore entries relating to writing off loss on issue of debentures and interest paid thereon.

[**Ans.** Debenture Redemption Investment ₹10,50,000 on 30th April, 2020; Debenture Redemption Reserve amounting to ₹7,00,000 will be transferred to General Reserve.]

Q. 12. Kuber Ltd. **(an unlisted company)** on 1st April 2015 acquired assets of the value of ₹7,00,000 and liabilities worth ₹80,000 from Varun Ltd., at an agreed value of ₹6,30,000. Kuber Ltd. issued 10% Debentures of ₹100 each at a premium of 5% in full satisfaction of purchase consideration. The debentures were redeemable on 31st October, 2020 at a premium of 4%. Pass journal entries to record the above including redemption of debentures.

[**Ans.** Goodwill ₹10,000; Debentures issued : 6,000 Debentures of ₹100 each. Debenture Redemption Reserve created for ₹60,000 on 31st March, 2015. Debenture Redemption Investment ₹90,000.]

Redemption of Debentures in Instalments by Drawing of Lots :

Q. 13. Universe Ltd. **(an unlisted company)** has 2,00,000, 9% debentures of ₹50 each due for redemption in five equal annual instalments starting from March 31, 2015. Debenture Redemption Reserve has a balance of ₹6,00,000. Record necessary journal entries.

[**Ans.** Amount transferred to Debenture Redemption Reserve ₹4,00,000 on 31st March, 2014. Investment made for ₹3,00,000 on 30th April, 2014 and encashed on 31st March, 2019. One-fifth of DRR will be transferred to General Reserve each time on redemption of one-fifth debentures.]

Q. 14. Priya Ltd. **(an unlisted company)** issued 30,000, 8% debentures of ₹200 each on August 1, 2011 redeemable as follows :

On 31st March, 2015	6,000 Debentures
On 31st March, 2016	7,000 Debentures
On 31st March, 2017	7,000 Debentures
On 31st March, 2018	10,000 Debentures

It was decided to transfer ₹1,75,000 each to Debenture Redemption Reserve on March 31, 2012 and March 31, 2013 and balance required to be transferred to Debenture Redemption Reserve on March 31, 2014. Record necessary journal entries. Ignore entries for payment of interest.

[**Ans.** Investment made for ₹1,80,000 on 30th April, 2014; ₹30,000 on 30th April 2015 and ₹90,000 on 30th April 2017 and entire amount of Investment ₹3,00,000 encashed on 31st March, 2018. Amount transferred to Debenture Redemption Reserve on March 31, 2014 ₹2,50,000; DRR transferred to General Reserve on 31st March 2015 ₹1,20,000; On 31st March 2016 ₹1,40,000; On 31st March 2017 ₹1,40,000; and On 31st March 2018 ₹2,00,000.]

Q. 15. Tata Power Ltd. **(an unlisted company)** issued 90,000, 9% Debentures of ₹100 each on July 1, 2014 redeemable at a premium of 5% as under :

On March 31, 2018	30,000 Debentures
On March 31, 2019	25,000 Debentures
On March 31, 2020	35,000 Debentures

It was decided to transfer to Debenture Redemption Reserve ₹2,00,000 on March 31, 2015; ₹3,00,000 on March 31, 2016 and the balance on March 31, 2017. Record necessary journal entries ignoring for interest.

[**Ans.** Investment made for ₹4,50,000 on 30th April 2017; Investment encashed for ₹75,000 on 31st March, 2018; Investment made for ₹1,50,000 on 30th April 2019; and Investment encashed for ₹5,25,000 on 31st March, 2020. Amount transferred to Debenture Redemption Reserve on March 31, 2017 ₹4,00,000; DRR transferred to General Reserve on 31st March 2018 ₹3,00,000; On 31st March 2019 ₹2,50,000; and on 31st March 2020 ₹3,50,000.]

Q. 16. On 1st April, 2019, the following balances appeared in the books of Uma Mahesh Ltd. *(an unlisted company)*

	₹
8% Debentures	24,00,000
Premium on Redemption of Debentures	1,20,000
Debenture Redemption Reserve	1,90,000

The debentures were to be redeemed at a premium of 5% in *two equal annual instalments* beginning from 31st March, 2021. The company transferred the balance amount to Debenture Redemption Reserve on 31st March, 2020. On 30th April, 2020, it met the requirements of the Companies Act, 2013 regarding Debenture Redemption Investment and redeemed the debentures on the scheduled dates.

You are required to pass necessary journal entries to record the above transactions in the books of the Company *(Ignore interest on Debentures).*

[Ans. Amount transferred to DRR on 31st March 2020 ₹50,000; Investment made for ₹1,80,000 on 30th April 2020 and encashed on 31st March 2022. DRR transferred to General Reserve ₹1,20,000 each on 31st March 2021 and 2022.]

Redemption of Debentures by Purchase of own Debentures in the open market

Q. 17. Sparrow Ltd. purchased its own 100, 10% debentures of ₹100 each from the open market for cancellation at ₹94.

You are required to pass journal entries for purchase and cancellation of own debentures. *(I.S.C. Specimen Question Paper, 2018)*

[Ans. Profit on Redemption ₹600.]

Note : It is assumed that the Company has adequate balance in DRR and must have invested the required amount.

Q. 18. *X* Ltd. purchased from open market its own 2,000, 9% Debentures of ₹100 each @₹102 per debenture for immediate cancellation. Pass Journal entries.

[Ans. Loss on cancellation ₹4,000 will be written off from Statement of Profit & Loss.]

Q. 19. On 1-4-2019 JJJ Ltd. had ₹1,00,00,000, 10% Debentures of ₹100 each outstanding.

(*i*) On 1-4-2020 the company purchased in the open market 30,000 of its own debentures for ₹99 each and cancelled the same immediately.

(*ii*) On 28-2-2021 the company redeemed at par debentures of ₹50,00,000 by draw of a lot.

(*iii*) On 31-1-2022 the remaining debentures were purchased for immediate cancellation for ₹20,03,000.

Ignoring interest on debentures, investments and debenture redemption reserve, pass necessary Journal entries for the above transactions in the books of the company.

[Ans. In Case (*i*) Gain on Redemption ₹30,000 transferred to Capital Reserve. In Case (*iii*) Loss on Redemption ₹3,000 written off from Statement of Profit & Loss.]

Q. 20. Voltas Ltd. purchased its own 4,000; 8% Debentures of ₹100 each @95 per debenture. These debentures were redeemable at 4% premium.

Pass necessary Journal entries for purchase and cancellation of debentures.

[Ans. Profit on cancellation ₹36,000 transferred to Capital Reserve.]

Q. 21. Manu Ltd. purchased from open market its own 5,000, 10% Debentures of ₹100 each @₹112 per debenture for immediate cancellation. These debentures were redeemable at 10% premium. Company has a balance of ₹15,000 in Capital Reserve.

Pass necessary Journal entries.

[Ans. Loss on cancellation ₹10,000 written off from Capital Reserve.]

Q. 22. Shashi Ltd. purchased for immediate cancellation its own 3,000, 9% Debentures of ₹100 each redeemable at 5% premium for ₹109 each. Company has a balance of ₹10,000 in its Capital Reserve.

Pass necessary Journal entries.

[**Ans.** Loss on cancellation written off from Capital Reserve ₹10,000 and from Statement of Profit & Loss ₹2,000.]

Q. 23. On 1st April, 2020, a company issued 2,000, 8% Debentures of ₹100 each at a premium of ₹20, repayable at a premium of ₹20. The terms of issue provided for the redemption of ₹20,000 debentures every year commencing from 31st March, 2022 either by purchase from the open market or by draw of lots at the company's option.

On 31st March, 2022, the company purchased for cancellation its own debentures of the face value of ₹16,000 at ₹95 per debenture and of ₹4,000 at ₹90 per debenture.

Show the Journal entries for redemption of debentures. Ignore entries relating to DRR and investments.

[**Ans.** Profit on cancellation transferred to Capital Reserve ₹5,200.]

Q. 24. *Z* Ltd. purchased for cancellation 2,000 of its own debentures of ₹100 each for ₹1,86,000 and 1,000 Debentures for ₹95,000. Expenses of purchase amounted to ₹1,500.

Pass journal entries ignoring DRR and investment.

[**Ans.** Profit on Redemption transferred to Capital Reserve ₹17,500.]

Q. 25. On 1st April, 2016, an unlisted Company made an issue of 5,000, 15% Debentures of ₹100 each. The terms of issue provided for the redemption of ₹1,00,000 Debentures annually, commencing from 31st March, 2018, either by drawing at par or by purchase in the market at the Company's option.

The Company transferred the required amount to DRR on 31st March, 2017 and invested the required amount on 30th April, 2017.

On 31st March, 2018, the Company purchased for cancellation 300 of its debentures at 95; 200 at 96 and 250 at 98. The expenses of purchase amounted to ₹320.

Record the redemption of debentures in the Company's Ledger for the year 2017-18, including interest on debentures.

[**Ans.** DRR created for ₹50,000; Debenture Redemption Investment ₹15,000 made on 30th April, 2017 will not be encashed. Profit on Redemption transferred to Capital Reserve ₹2,480. Proportionate amount of DRR transferred to General Reserve ₹10,000.]

Q. 26. On 1st April, 2015, an unlisted company made an issue of 20,000, 8% debentures of ₹100 each at ₹106 per debenture. The terms of issue provided for the redemption of ₹5,00,000 debentures every year commencing from 31st March, 2018 either by purchase or by drawings at par at the company's option.

Company transferred the required amount to DRR and invested the required amount as per law.

On 31st March, 2018, the company purchased for cancellation debentures of the face value of ₹3,00,000 at ₹90 per debenture and of ₹2,00,000 at ₹95 per debenture. Journalise the above transactions and show how the profit on redemption would be treated.

[**Ans.** DRR created on 31st March, 2017 ₹2,00,000; Debenture Redemption Investment ₹75,000 made on 30th April, 2017 will not be encashed. Profit on

Redemption ₹40,000; Proportionate amount of DRR transferred to General Reserve ₹50,000.]

Hint : Profit on redemption of debentures ₹40,000 will be transferred to Capital Reserve Account.

Purchase of Own Debentures as Investment :

Q. 27. India Tea Ltd. (an unlisted company) purchased for cancellation its 800, 13% Debentures of ₹100 each at ₹95. (*i*) Make journal entries, (*ii*) What journal entry will be made if debentures are purchased as investments. Ignore entries relating to DRR and investment of 15% amount.

[**Ans.** Profit on Redemption ₹4,000 in case (*i*).]

Q. 28. Mafatlal Cotton Ltd. (an unlisted company) has an outstanding balance of 5,000, 9% debentures of ₹100 each. The Board of Directors decided to purchase 4,000 of its own debentures at a price of ₹94 for investments purpose. But after few months they took decision to sell them @ ₹97 in the market. Record necessary entries to show above transactions.

[**Ans.** Profit on sale of investment in Own debentures transferred to Statement of Profit and Loss ₹12,000.]

Note : The Company is not required to create DRR and also there is no requirement to make investment because the debentures are purchased for investment and not for cancellation.

Q. 29. *X* Ltd. purchased its 5,000, 8% debentures of ₹100 at ₹95 for investment on 1st October, 2020. Expenses amounted to ₹4,000. On 1st January, 2021, it sold 4,000 of its debentures at ₹98 per debenture. Expenses amounted to ₹3,000. On 31st March, 2021, it decided to cancel the rest of the debentures.

Journalise these transactions in the book of *X* Ltd.

[**Ans.** Investment in Own Debentures ₹4,79,000; Profit on sale of Own Debentures ₹5,800; Profit on Cancellation ₹4,200.]

Note : It is assumed that the Company has sufficient balance in DRR.

Q. 30. On 1st April 2020, Nikita Ltd. had 10,000, 12% Debentures of ₹100 each. On the same date it purchased 3,000 of its own debentures from the open market for ₹2,95,000, expenses of purchase being ₹500.

The debentures were held as investment till 31st March, 2021 when it decided to cancel them. Interest is payable half yearly on 30th September and 31st March and the books are closed on 31st March every year.

Pass journal entries in the books of the company.

[**Ans.** Profit on cancellation of Debentures ₹4,500.]

Hint :

Interest on Sept. 30, 2020 : ₹42,000 on Outside Debentures plus ₹18,000 on Own Debentures.
Interest on Mar. 31, 2021 : ₹42,000 on Outside Debentures plus ₹18,000 on Own Debentures.

Note : It is assumed that the Company has sufficient balance in DRR.

Additional Questions (For Practice)

Lump-sum Payment at the end of Fixed Period :

Q. 31. On 1st April, 2015, Mayfair Ltd. (an unlisted company) issued 4,000 9% debentures of ₹100 each at a discount of 5% redeemable at a premium of 8%. The debentures were redeemable on 31st March, 2019.

The company created the necessary minimum amount of debenture redemption reserve and purchased the required amount of debenture redemption investments as per the provisions of Companies Act, 2013.

Pass the necessary journal entries for issue and redemption of debentures.

(C.B.S.E. 2020, Delhi)

[**Ans.** Debenture Redemption Reserve created for ₹40,000 on 31st March 2018. Debenture Redemption Investment for ₹60,000 made on 30th April 2018.]

Q. 32. Eagle Ltd. (an unlisted company) has 3,000; 10% Debentures of ₹100 each outstanding as on 31st March, 2019. These debentures are due for redemption on 31st March, 2020. The Debenture Redemption Reserve has a balance of ₹10,000 on 31st March, 2019.

You are required to pass journal entries to complete the redemption of Debentures.

[**Ans.** ₹20,000 will be transferred from Surplus in Statement of P & L to Debenture Redemption Reserve A/c on 31st March, 2019. Debenture Redemption Investment made for ₹45,000 on 30th April, 2019. Balance of DRR ₹30,000 will be transferred to General Reserve.]

Q. 33. Ruchi Ltd. (an unlisted company) issued 42,000, 7% Debentures of ₹100 each on 1st April, 2016, redeemable at a premium of 8% on 31st March 2020. The Company decided to create required Debenture Redemption Reserve on 31st March 2019. The company invested the funds as required by law in a fixed deposit with State Bank of India on 1st April, 2019 earning interest @10% per annum. Tax was deducted at source by the bank on interest @10%. Pass necessary Journal Entries regarding issue and redemption of debentures.

[**Ans.** Amount transferred to Debenture Redemption Reserve ₹4,20,000 on 31st March, 2019; Debenture Redemption Investment ₹6,30,000 on 1st April, 2019; Interest Received ₹63,000.]

Q. 34. Krishna Ltd. (an unlisted company) has issued 20,000, 9% Debentures of ₹100 each of which half the amount is due for redemption on March 31st 2018. It was decided to invest the required amount towards Debenture Redemption Investment. The company has in its Debenture Redemption Reserve Account a balance of ₹1,20,000 on 31st March, 2017. Record the necessary journal entries for the Redemption of Debentures.

(C.B.S.E. 2019, M.P.)

[**Ans.** Amount transferred to Debenture Redemption Reserve on 31st March, 2017 ₹80,000. Debenture Redemption Investment ₹1,50,000. DRR transferred to General Reserve ₹1,00,000.]

Hint : One half of Debenture Redemption Reserve will be transferred to General Reserve A/c since one-half debentures are redeemed.

Q. 35. Saraswati Ltd. (an unlisted company) issued 8,000, 9% debentures of ₹200 each at premium of 5% on June 30, 2010, redeemable on July 1, 2020. The Board of Directors decided to transfer ₹60,000 to Debenture Redemption Reserve on March 31, 2019 and balance on March 31, 2020. Record necessary entries for the issue as well as at the time of redemption of debentures. Ignore entries for payment of interest.

[**Ans.** Debenture Redemption Investment made for ₹2,40,000 on 30th April, 2020. Debenture Redemption Reserve transferred to General Reserve ₹1,60,000.]

Q. 36. Pooja Ltd. (an unlisted company) issued 80,000, 8% debentures of ₹100 each on June 30, 2016 redeemable at a premium of 6% on July 1, 2020. The Board of Directors have decided to transfer out of profits ₹3,00,000 to Debenture Redemption Reserve on March 31, 2018, ₹3,00,000 on March 31, 2019 and balance on March 31, 2020. Record necessary journal entries regarding issue and redemption of debentures. Ignore entries relating to writing off loss on issue of debenture and interest paid thereon.

[**Ans.** Debenture Redemption Investment made for ₹12,00,000 on 30th April, 2020. Debenture Redemption Reserve transferred to General Reserve ₹8,00,000 on July, 1, 2020.]

Purchase of Own Debentures

Q. 37. ABC Ltd. Purchased for cancellation its own 5,000, 9% Debentures of ₹100 each for ₹95 per debenture. The brokerage charges ₹15,000 were incurred.

Calculate the amount to be transferred to Capital Reserve.

(C.B.S.E. Sample Paper, 2017)

[**Ans.** Amount transferred to Capital Reserve ₹10,000.]

Q. 38. On 1st April, 2019, an unlisted company issued 10,000, 9% debentures of ₹100 each at a premium of 5%. The terms of issue provide for redemption of ₹1,00,000 worth of Debentures every year commencing from March, 2022 either by purchasing in the open market or by draw of lots at the company's option.

The Company transferred the required amount to DRR and invested the required amount as per law.

On 31st March, 2022, the company purchased 400 debentures @ ₹95 and 500 Debentures @ ₹96 for cancellation and redeemed the balance of ₹10,000 debentures by draw of lots. Journalise these transactions and also show how you would deal with the profit on redemption of debentures.

[**Ans.** DRR created for ₹1,00,000 on 31st March 2021; Debenture Redemption Investment made on 30th April, 2021 for ₹15,000 and will not be encashed. Profit on redemption ₹4,000 will be transferred to capital reserve. Proportionate amount of DRR *i.e.,* ₹10,000 will be transferred to General Reserve.]

Q. 39. *A* Ltd. purchased for cancellation ₹2,50,000 of its 12% Debentures at ₹92. The brokerage being 1%. Journalise.

[**Ans.** Profit on Redemption ₹17,700 will be transferred to Capital Reserve.]

Q. 40. *Y* Ltd. (an unlisted company) issued 6,000, 13% Debentures of ₹100 each on 1st April, 2015 at par. The terms of Debentures Trust Deed provided for the redemption of ₹1,50,000 annually commencing from March, 2020 either by drawings at par or by purchase in the open market at the company's option.

The Company transferred the required amount to DRR and invested the required amount as per Law.

On 31st March, 2020, the Company purchased ₹ 1,20,000 of its Debentures at ₹95 and incurred the brokerage @ 2%. Prepare necessary accounts for the year 2019-20.

Y Ltd.

Ans.

OWN DEBENTURES A/C

Dr. Cr.

Date	Particulars	₹	Date	Particulars	₹
2020 Mar. 31	To Bank A/c (₹1,14,000 + 2% brokerage)	1,16,280	2020 Mar. 31	By 13% Debentures A/c	1,16,280

13% DEBENTURES A/C

Dr. Cr.

Date	Particulars	₹	Date	Particulars	₹
2020 Mar. 31	To Own Debentures A/c (1,14,000 + 2% brokerage)	1,16,280	2019 April 1	By Balance b/d	6,00,000
Mar. 31	To Profit on Redemption A/c (1,20,000 – 1,16,280)	3,720			
Mar. 31	To Debentureholders A/c (drawings)	30,000			
Mar. 31	To Balance c/d	4,50,000			
		6,00,000			6,00,000

PROFIT ON REDEMPTION A/C

Dr. Cr.

Date	Particulars	₹	Date	Particulars	₹
2020 Mar. 31	To Capital Reserve A/c	3,720	2020 Mar. 31	By 13% Debentures A/c	3,720

DEBENTURE REDEMPTION INVESTMENT A/C

Dr. Cr.

Date	Particulars	₹	Date	Particulars	₹
2019 Apr. 30	To Bank A/c (15% of ₹1,50,000)	22,500	2020 Mar. 31	By Balance c/d	22,500

DEBENTURE REDEMPTION RESERVE A/C

Dr. Cr.

Date	Particulars	₹	Date	Particulars	₹
2020 Mar. 31	To General Reserve A/c*	15,000	2019 April 1	By Balance b/d (10% of ₹6,00,000)	60,000
Mar. 31	To Balance c/d	45,000			
		60,000			60,000

*Since ₹1,50,000 out of total debentures of ₹6,00,000 have been redeemed, one-fourth of DRR has been transferred to General Reserve A/c.

Q. 41. On 1st April, 2016, *X* Ltd. (an unlisted company) made an issue of 8,000, 11% debentures of ₹100 each. According to the terms of issue, debentures of the face value of ₹1,00,000 are to be redeemed annually commencing from March, 2022, either by drawings at par or by purchase in the open market.

The Company transferred the required amount to DRR and invested the required amount as per law.

On 31st March, 2022, the Company purchased for cancellation ₹50,000 debentures at ₹96 and ₹30,000 debentures at ₹95 and redeemed the balance by draw of lots. The expenses on purchase amounted to ₹1,200. Prepare necessary accounts for the year ending 31st March, 2022.

[Ans. Debenture Redemption Reserve created on 31st March 2021 for ₹80,000. Debenture Redemption Investment ₹15,000 made on 30th April, 2021 and will not be encashed. Profit on Redemption transferred to Capital Reserve ₹2,300; Proportionate amount of DRR transferred to General Reserve ₹10,000.]

Multiple Choice Questions

Select the Best Alternate and tally your answer with the Answers given at the end of the book :

Q. 1. As per SEBI Guidelines in case of an unlisted company, an amount equal to .... of the debentures outstanding must be transferred to Debenture Redemption Reserve before redemption begins.

(A) 25%	(B) 50%
(C) 10%	(D) 100%

Q. 2. A company issuing debentures with a maturity period of not more than 18 months, in that case the creation of Debenture Redemption Reserve will be :

(A) 10% of the amount of debentures outstanding

(B) 25% of the amount of debentures outstanding

(C) 50% of the amount of debentures outstanding

(D) None of the above

Q. 3. According to the guidelines issued by Securities and Exchange Board of India (SEBI) what percentage of the amount of debentures must be transferred to 'Debenture Redemption Reserve' before the commencement of redemption of debentures, in case of convertible debentures?

(A) 25%	(B) 50%
(C) 100%	(D) Zero

Q. 4. Utsav Ltd. (an unlisted company) decided to redeem its 4,000, 9% Debentures of ₹100 each which were issued at a discount of 8%, and were redeemable at a premium of 10%. The amount transferred to Debenture Redemption Reserve will be :

(A) ₹ 40,800	(B) ₹44,000
(C) ₹1,00,000	(D) ₹40,000

(C.B.S.E. 2020, Kolkata, Lucknow)

Q. 5. *X* Ltd. (an unlisted company) wants to redeem 5,000, 5% Debentures of ₹100 each at 5% premium. How much amount it must transfer to Debenture

Redemption Reserve, if it has already a balance of ₹20,000 in Debenture Redemption Reserve Account?

(A) ₹1,05,000 (B) ₹ 30,000
(C) ₹2,30,000 (D) ₹4,80,000

Q. 6. A Company issuing debentures with a maturity period of not more than .... need not create Debenture Redemption Reserve.

(A) 2 months (B) 6 months
(C) 12 months (D) 18 months

Q. 7. Where is 'Debenture Redemption Reserve' transferred after the redemption of all debentures?

(A) Capital Reserve Account (B) General Reserve Account
(C) Statement of Profit and Loss (D) Sinking Fund Account

Q. 8. Wellness Co. Ltd. (an unlisted company) has issued 20,000, 9% Debentures of ₹100 each at a premium of 10% on 1st April, 2018 redeemable as follows:

31st March, 2021 — 10,000 debentures
31st March, 2022 — 4,000 debentures
31st March, 2023 — balance debentures.

It transferred the required amount to Debentures Redemption Reserve on due date. How much amount will be transferred to General Reserve on 31st March, 2021

(A) ₹2,50,000 (B) ₹1,00,000
(C) ₹2,00,000 (C) ₹5,00,000

(C.B.S.E. Sample Paper, 2020)

Q. 9. No debenture redemption reserve is required for debentures issued by :

(A) Manufacturing Companies (B) Infrastructure Companies
(C) Banking Companies (D) Trading Companies

(C.B.S.E. 2020, Kerala)

Q. 10. Premier Ltd. issued 2,000, 9% Debentures of ₹100 each at par, redeemable after five years at a premium of 10%. The minimum amount invested in Debenture Redemption Investments will be :

(A) ₹30,000 (B) ₹ 33,000
(C) ₹50,000 (D) ₹2,00,000

(C.B.S.E. 2020, Rajasthan)

(See answers at the end of the book.)

9

Financial Statements of Companies

LEARNING OBJECTIVES

After studying this Chapter you should be able to understand :

- **Meaning of Financial Statements**
- **Nature of Financial Statements**
- **Schedule III for preparing Balance Sheet and Statement of Profit and Loss**
- **Types of Reserves**
- **Divisible Profits**
- **Preparation of Balance Sheet**

Meaning of Financial Statements

Financial statements are the end products of accounting process. They provide information about the profitability and the financial position of a business.

Financial Statements :

As per Section 2 (40) of the Companies Act, 2013, the ''Financial Statements'' in relation to a Company, include the following :

(*i*) A balance sheet as at the end of the financial year;

(*ii*) A statement of profit and loss for the financial year;

(*iii*) Cash flow statement for the financial year;

(*iv*) A statement of changes in equity, if applicable; and

(*v*) Explanatory notes.

Financial Year :

As per Section 2 (41) of the Companies Act, 2013, all companies are required to have a uniform financial year which shall be a period from 1st April to 31st March every year. Only companies which are a holding or subsidiary of a foreign company required to follow different financial year for the purposes of consolidation of its accounts outside India may apply to the Tribunal for a different financial year.

Section 129 (1) of the Companies Act 2013, requires that the financial statements of a Company,

(*i*) shall give a true and fair view of the state of affairs of the Company, (*ii*) should comply with the accounting standards notified under section 133 and

(*iii*) shall be in the prescribed form given in Schedule III.

The prescribed form for the preparation of balance sheet has been given in Part I of Schedule III and prescribed form for the preparation of Statement of Profit & Loss has been given in Part II of Schedule III.

The Board of Directors shall present the financial statements before the shareholders for their approval, at every Annual General Meeting of the Company. The auditor's report and director's report must be attached to the financial statements of the Company.

Objectives of Preparing Financial Statements :

(*i*) To present a true and fair view of the financial performance (*i.e.* profit/loss) of the business;

(*ii*) To present a true and fair view of the financial position (*i.e.* Assets/Equity & Liabilities) of the business.

Characteristics of Financial Statements

(*i*) Financial statements are related to past period and hence are historical documents.

(*ii*) They are expressed in terms of money.

(*iii*) Financial statements show profitability through Statement of Profit and Loss and financial position through Balance Sheet.

Characteristics of Balance Sheet :

(*i*) It portrays the relationship between Equity & Liabilities and Assets. Total of Equity & Liabilities side is always equal to the assets side.

(*ii*) It is prepared on a particular date and not for a period. It is true only for the date on which it is prepared because even a single transaction would cause a change in assets and liabilities.

(*iii*) It shows the financial position of the business according to the going concern concept.

(*iv*) It is not based on absolute facts but is influenced by accounting assumptions and personal judgements.

Characteristics of Statement of Profit and Loss

(*i*) It matches the revenues and expenses of an enterprise for a particular period in order to determine the profit earned or loss suffered during the period.

(*ii*) It is prepared for a particular period and not on a particular date.

(*iii*) It is prepared for a past period and hence it is a historical document.

Nature of Financial Statements

Data exhibited in the financial statements are not absolute facts because they are affected by recorded facts, accounting conventions and personal judgements :

(1) **Recorded Facts** : The term recorded facts means that the data used for preparing financial statements are drawn from accounting records. For example, figures relating to cash in hand, cash at bank, trade receivables, cost of fixed assets etc. are recorded facts. The financial statements do not include such facts which are not recorded in the books whether or not such facts are significant. The assets purchased at different times and at different prices are shown in the Balance Sheet at their actual cost. They are not shown in the Balance Sheet at their realisable value or replacement cost because as per the accounting records the cost price (not the realisable value or replacement cost) of the fixed cost is a recorded fact.

(2) **Accounting Conventions** : Accounting Conventions imply certain fundamental accounting principles which have gained wide acceptance and which are followed while preparing financial statements. For example, due to the convention of 'Conservatism', provision is made in the books for expected future losses but expected profits are ignored. Likewise, the closing inventory is valued at cost or realisable value whichever is less. This means that the actual financial position of the business may be much better than disclosed by financial statements.

(3) **Personal Judgements** : Even though certain accounting conventions are followed while preparing the financial statements, still personal judgement of the accountant plays a decisive role in accounting. For example, the accountant has to decide whether the asset is to be depreciated on straight line method, written down value method or some other method. He is to apply his personal judgement in deciding the rate of depreciation also. Likewise, though the inventory is valued at cost or realisable value whichever is less but there are a number of methods for valuing the inventory at cost such as First in First out, Last in First out, Average cost, Standard cost etc. Accountant can choose any of these methods. Similarly, the accountant has to exercise his personal judgement in respect of rate of provision for doubtful debts, period for writing off intangible assets and classification of expenditure into capital and revenue.

Schedule III for preparing Balance Sheet and Statement of Profit and Loss

Balance Sheet and Statement of Profit and Loss of a Company must be prepared as per the format given in Schedule III.

Schedule III does not offer any horizontal format. The new vertical format is as follows :

PART I

FORMAT OF BALANCE SHEET

Name of the Company ....

Balance Sheet as at .... *(₹ in ....)*

Particulars *1*	*Note No.* *2*	*Figures as at the end of current reporting period* *3*	*Figures as at the end of the previous reporting period* *4*
I. EQUITY AND LIABILITIES			
(1) Shareholders' funds			

(*a*) Share capital			
(*b*) Reserves and surplus			
(*c*) Money received against share warrants			
(2) **Share application money pending allotment**			
(3) **Non-current liabilities**			
(*a*) Long-term borrowings			
(*b*) Deferred tax liabilities (net)			
(*c*) Other Long-term liabilities			
(*d*) Long-term provisions			
(4) **Current liabilities**			
(*a*) Short-term borrowings			
(*b*) Trade payables			
(*c*) Other current liabilities			
(*d*) Short-term provisions			
TOTAL			
II. ASSETS			
(1) **Non-current assets**			
(*a*) Fixed Assets			
(*i*) Tangible assets			
(*ii*) Intangible assets			
(*iii*) Capital work-in-progress			
(*iv*) Intangible assets under development			
(*b*) Non-current investments			
(*c*) Deferred tax assets (net)			
(*d*) Long-term loans and advances			
(*e*) Other non-current assets			
(2) **Current assets**			
(*a*) Current investments			
(*b*) Inventories			
(*c*) Trade receivables			
(*d*) Cash and Bank Balance			
(*e*) Short-term loans and advances			
(*f*) Other current assets			
TOTAL			

Distinction between a Company's Balance Sheet and a Firm's Balance Sheet :

	Basis of Distinction	*Company's Balance Sheet*	*Firm's Balance Sheet*
1.	**Format and Contents**	Format and Contents of a Company's Balance Sheet must be in accordance with Schedule III Part I of Company's Act 2013.	There is no statutory format or prescribed contents for the Balance Sheet of a firm.
2.	**Figures of Previous Year**	Figures of the previous year must also be given against each figure of current year.	Figures of the previous year are not required in the Balance Sheet of a firm.

3. **Order of Permanence or Liquidity**	Company's Balance Sheet is prepared in order of permanence.	Firm's Balance Sheet may be prepared in order of permanence or liquidity.
4. **Vertical form or Horizontal form**	Company's Balance Sheet is prepared in Vertical form.	Firm's Balance Sheet is generally prepared in horizontal form.

IMPORTANT NOTE

Certain items have been marked with**.

** The students are required to know the meaning and the heading/sub-heading under which these items will appear in the Balance Sheet.

*However, for all items marked with ** no accounting treatment will be asked.*

Notes : General Instructions for Preparation of Balance Sheet :

1. **An asset shall be classified as current** when it satisfies any of the following criteria :
   - (*a*) it is expected to be realized in, or is intended for sale or consumption in, the company's normal operating cycle;
   - (*b*) it is held primarily for the purpose of being traded;
   - (*c*) it is expected to be realized within twelve months after the reporting date.

   All other assets shall be classified as non-current.
2. An operating cycle is the time between the acquisition of assets for processing and their realization in cash or cash equivalents. Where the normal operating cycle cannot be identified, it is assumed to have a duration of 12 months.
3. **A liability shall be classified as current** when it satisfies any of the following criteria :
   - (*a*) it is expected to be settled in the company's normal operating cycle;
   - (*b*) it is held primarily for the purpose of being traded;
   - (*c*) it is due to be settled within twelve months after the reporting date.

   All other liabilities shall be classified as non-current.
4. **No debit balance of profit and loss along with assets :** An important change in the Schedule III is elimination of debit balance of Profit and Loss statement from the assets. It is now to be presented as negative balance within "Reserves and Surplus."
5. **Treatment of Miscellaneous Expenditure :** As per AS-16 Borrowing Costs and discount or premium on redemption relating to borrowing could be amortized over loan period. Further, share issue expenses, underwriting commission, discount on debentures, premium on redemption etc., being special nature items are excluded from the scope of AS-26 (Intangible Assets). These items can be amortized over the period of benefit, *i.e.*, normaly 3 to 5 years.

6. The Schedule III has eliminated the Concept of 'Schedules' and henceforth such information is to be furnished in terms of 'Notes to Accounts'

7. The Schedule III requires that on the face of the Balance Sheet and Statement of Profit & Loss, only one amount shall be shown against each item and details of that item shall be given in note relating to the item. For example, share capital will be shown as one amount on the face of the Balance Sheet writing No. 1 in the Note No. Column and the details of Share Capital will be given in Notes to Accounts under Note 1

8. As per Schedule III if a Balance Sheet is to be prepared for example on 31st March, 2022, then the date of Balance Sheet will be stated 'as at 31st March, 2022' and not 'as on 31st March, 2022'. This is because the word 'On' refers to the entire duration of the day consisting of 24 hours whereas the word 'At' refers to a particular point of time. Since the Balance Sheet is prepared to depict the financial position of the enterprise at a particular point of time i.e. at the end of day's business hours, the word 'At' should be used instead of 'On'.

Explanation of Equity and Liabilities

(1) Shareholder's Funds :

(A) Share Capital : Under the head, 'Share Capital', some of the important items to be shown are as under :

The disclosure of Share Capital in the Balance Sheet is limited to the following :

Name of the Company ....
Balance Sheet (An extract) as at ....

(₹ in ....)

Particulars	Note No.	Figures as at the end of current reporting period	Figures as at the end of the previous reporting period
I. EQUITY AND LIABILITIES :		₹	₹
1. **Shareholder's Funds :**			
(*a*) Share Capital	1	....	....

Notes to Accounts (1)

	Amount
(*a*) **Share Capital :**	₹
Authorised Capital	
.... Shares of ₹....... each	....
Issued Capital	
.... Shares of ₹....... each	....

(of the above shares .... shares are allotted as fully paid up pursuant to a contract without payment being received in cash)		
Subscribed Capital		
Subscribed and fully paid up		
.... Shares of ₹....... each	....	
(of the above shares .... shares are allotted as fully paid up pursuant to a contract without payment being received in cash)		
Subscribed but not fully paid up		
.... Shares of ₹....... each .... Called up		
Less : Calls-in-Arrears	....	
	....	
Add : Shares forfeited A/c	....	....

Note : (1) Equity share capital and Preference share capital to be shown separately.

(2) If the authorised / issued capital is not mentioned in the question it has to be shown in the notes to accounts. However, no figures will be shown as illustrated above.

(B) **Reserves and Surplus**

The following items are shown under this head :

(*i*) Reserves and Surplus shall be classified as :

(*a*) Capital Reserves;

(*b*) Capital Redemption Reserve;**

(*c*) Securities Premium Reserve;

It shall be used to write off the items under Section 52 of the Companies Act 2013 and the balance if any will be shown under the head 'Reserve and Surplus'.

Notes to Accounts :

Particulars		*Amount (₹)*
Securities Premium Reserve	XXX	
Less : Discount on issue of debentures (arising in the year in which it occurs) written off	(xx)	XXX

Under Section 52 of the Companies Act, 2013 Securities Premium can be utilised for the following purposes :

(*i*) for issuing fully paid bonus shares.

(*ii*) for writing off preliminary expenses.

(*iii*) for writing off issue expenses or underwriting commission or discount allowed on issue.

(*iv*) for providing premium payable on redemption of pref. shares or debentures.

(*v*) for buy back of its own shares or other securities under Section 68.

(*d*) Debenture Redemption Reserve;

(*e*) Revaluation Reserve**

(*f*) Share Options Outstanding Account : It is a form of employee compensation wherein employees are offered an option to apply and get allotment of Company's shares at a future date at a specified price which is usually sufficiently below the market price of the share.**

(*g*) Other Reserves (Restricted to General Reserve only).

(*h*) Surplus, *i.e.*, balance in Statement of Profit & Loss after appropriations such as dividend, bonus shares and transfer to/from reserves etc.

(Schedule III does not provide for preparation of Profit & Loss Appropriation Account. This means the Appropriations should be presented in the Notes to Accounts.)

(*ii*) Debit balance of statement of profit and loss shall be shown as a negative figure under the head 'Surplus'. Similarly, the balance of 'Reserves and Surplus', after adjusting negative balance of surplus, if any, shall be shown under the head 'Reserves and Surplus' even if the resulting figure is in the negative.

ILLUSTRATION : 1.

Olympus Ltd. has an opening debit balance of ₹5,00,000 in Reserves and Surplus as Balance of Statement of Profit & Loss. It earned a profit of ₹8,00,000 for the year ended 31st March, 2020. How would you show these items in the Balance Sheet and notes to accounts?

SOLUTION :

Olympus Ltd.

EXTRACT OF BALANCE SHEET

as at 31st March, 2020

Particulars	*Note No.*	*31.03.2020*	*31.03.2019*
I. EQUITY AND LIABILITIES :		₹	₹
(1) **Shareholder's Funds**			
Reserves and Surplus	1	3,00,000	(5,00,000)

Notes to Accounts :

		31.03.202
(1) Reserves and Surplus :		₹
Surplus		
Balance in Statement of Profit & Loss (Opening)	(5,00,000)	
Surplus for the period	8,00,000	3,00,00

ILLUSTRATION : 2.

Galaxy Ltd. has the following balances on 1st April, 2019 :

	₹
General Reserve	4,50,000
Statement of Profit & Loss	2,00,000

During the year ended 31st March, 2020, it incurred a loss of ₹3,20,000. How would you show these items in the Balance Sheet and notes to accounts?

SOLUTION :

Galaxy Ltd.

EXTRACT OF BALANCE SHEET

as at 31st March, 2020

Particulars	*Note No.*	*31.03.2020*	*31.03.2019*
I. EQUITY AND LIABILITIES :		₹	₹
(1) **Shareholder's Funds :**			
Reserves and Surplus	1	3,30,000	6,50,000

Notes to Accounts :

		31.03.2020
(1) Reserves and Surplus :		₹
(*a*) General Reserve		4,50,000
(*b*) Surplus :		
Balance in Statement of Profit & Loss (Opening)	2,00,000	
Surplus (Loss) for the Period	(3,20,000)	(1,20,000)
		3,30,000

ILLUSTRATION : 3.

Royal Ltd. has the following balances on 1st April, 2019 :

	₹
General Reserve	2,00,000
Securities Premium Reserve	1,00,000
Statement of Profit & Loss	(7,00,000)

During the year ended 31st March, 2020, it incurred a loss of ₹4,50,000. Show how these items will appear in the Balance Sheet and notes to accounts.

SOLUTION :

Royal Ltd.

EXTRACT OF BALANCE SHEET

as at 31st March, 2020

Particulars	*Note No.*	*31.03.2020*	*31.03.2019*
I. EQUITY AND LIABILITIES :		₹	₹
(1) **Shareholder's Funds :**			
Reserves and Surplus	1	(8,50,000)	(4,00,000)

Notes to Accounts :

		31.03.2020
		₹
(1) Reserves and Surplus :		
(*a*) Securities Premium Reserve		1,00,000
(*b*) General Reserve		2,00,000
(*c*) Surplus :		
Balance in Statement of Profit & Loss (Opening)	(7,00,000)	
Surplus (Loss) for the Period	(4,50,000)	(11,50,000)
		(8,50,000)

ILLUSTRATION : 4.

Kotak Ltd. has the following balances on 1st April, 2019 :

	₹
Statement of Profit & Loss	(2,00,000)
Debenture Redemption Reserve	6,00,000
Capital Reserve	5,00,000

It earned a profit of ₹10,00,000 for the year ended 31st March, 2020. It decided to transfer ₹2,00,000 to Debenture Redemption Reserve and ₹3,00,000 to General Reserve.

Show how these items will appear in the Balance Sheet and notes to accounts.

SOLUTION :

Kotak Ltd.

EXTRACT OF BALANCE SHEET

as at 31st March, 2020

Particulars	*Note No.*	*31.03.2020*	*31.03.2019*
I. EQUITY AND LIABILITIES :		₹	₹
(1) **Shareholder's Funds :**			
Reserves and Surplus	1	19,00,000	9,00,000

Notes to Accounts :

		31.03.2020
(1) Reserves and Surplus :		₹
(*a*) Capital Reserve		5,00,000
(*b*) Debenture Redemption Reserve :		
Opening Balance	6,00,000	
Transfer from Surplus	2,00,000	8,00,000
(*c*) General Reserve :		
Opening Balance	—	
Transfer from Surplus	3,00,000	3,00,000
(*d*) Surplus :		
Balance in Statement of Profit & Loss (Opening)	(2,00,000)	

Surplus for the Period		10,00,000	
Available for Appropriations		8,00,000	
Less : Appropriations :			
Debenture Redemption Reserve	2,00,000		
General Reserve	3,00,000	5,00,000	3,00,000
			19,00,000

(C) **Money Received against share warrants**** : A share warrant is a financial instrument issued by a public company which gives the holder the right to acquire certain number of equity shares specified therein at a later date. Amount received against share warrants is included in shareholder's funds as they will be converted into equity shares on specified date at a pre-determined price. These are not shown as part of share capital but to be shown as a separate line item.

(Students need to know only its meaning and under which heading / sub-heading this item appear in Schedule III)

(2) **Share Application money pending allotment**** : If a company has received application money but date of allotment falls after the Balance Sheet date, such application money pending allotment will be shown in the following manner :

(*i*) Share application money not exceeding the issued capital and to extent not refundable is to be disclosed under this line-item.

(*ii*) Share application money to the extent refundable or where minimum subscription is not met, such amount shall be shown separately under 'Other Current Liabilities'.

(Students need to know only its meaning and under which heading / sub-heading this item appear in Schedule III)

(3) **Non-Current Liabilities** : A non-current liability is a liability which is not classified as current liability. Non-Current Liabilities shall be classified as follows :

(A) **Long-term Borrowings** : Long-term borrowings shall be classified as :

(*a*) **Long term Borrowings** : Borrowings refer to loans taken by the Company. Borrowings shall be classified as long-term borrowings when they are payable by the company after 12 months from the date of the loan. It shall be shown under the following heads :

(*i*) Bonds/Debentures

(*ii*) Premium Payable on Redemption of Debentures

(*iii*) Long Term Loans

- From Banks.
- From Other Parties.

(*iv*) Fixed Deposits/Public Deposits

(*v*) Other Loans and Advances

Some part of the Long term Borrowings may be due for payment within 12 months from the date of Balance Sheet. It will be shown under 'Other Current Liabilities' as Current Maturities of Long term Debts.

(B) **Deferred tax liabilities (Net)****
(Students need to know only its meaning and under which heading / sub-heading this item appear in Schedule III)

Deferred Taxes :

Taxable income is different from Accounting income. Taxable income is the income based on tax laws whereas Accounting income is determined as per the accounting practices followed in the enterprise. Accounting income is reported by statement of profit and loss of the enterprise. The current practice has been to make 'provision for tax' on the Taxable income. However, tax can also be calculated on the accounting income. The difference between tax on Accounting income and Taxable income is called 'deferred tax'.

Deferred Tax Liabilities :

A deferred tax liability comes into existence when accounting income is more than taxable income.

(C) **Other Long-term Liabilities****

(D) **Long-term provisions** : Provision is the amount set aside to meet future liabilities, the amount of which cannot be determined with reasonable accuracy. All provisions for which the related claims are expected to be settled beyond 12 months after the Balance Sheet date are classified as long-term provisions. Examples are Provision for Employee Benefits**, Provision for Warranties** etc.

(4) **Current Liabilities : A Liability shall be classified as current** when it satisfies any of the following criteria :

(*i*) it is expected to be settled in the company's normal operating cycle; or

(*ii*) it is held primarily for the purpose of being traded; or

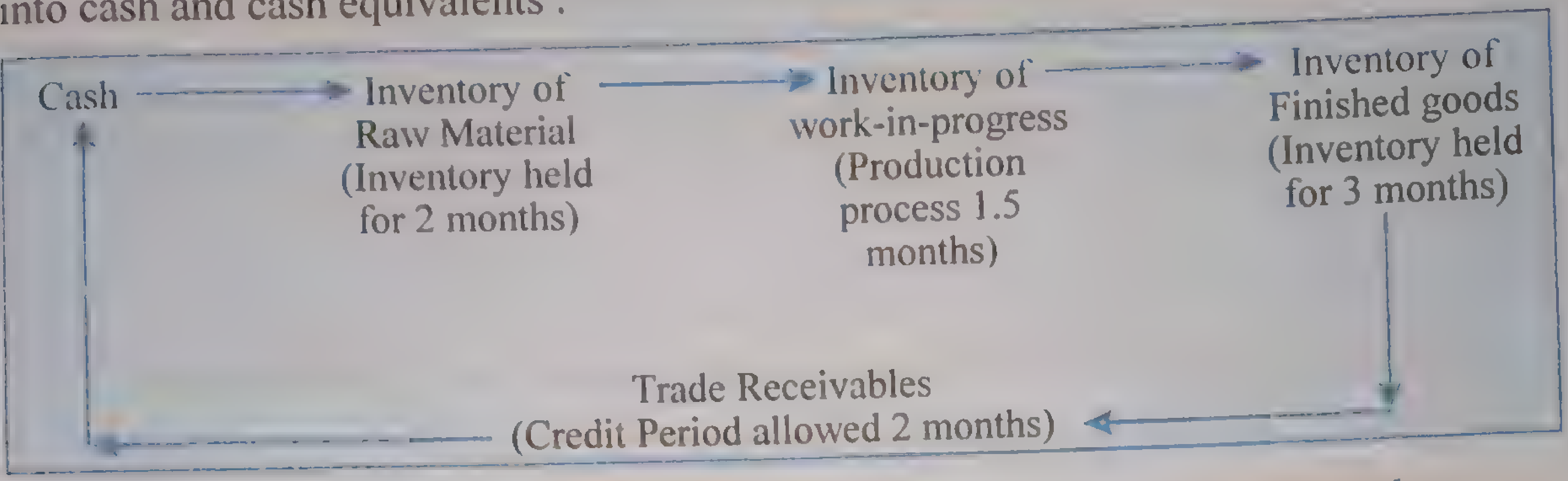
(*iii*) it is due to be settled within twelve months after the reporting date (i.e. Balance Sheet date) or

(*iv*) the company does not have an unconditional right to defer settlement of the liability for atleast 12 months after the reporting date. (i.e. Balance Sheet date).

If a liability is expected to be settled within the Company's normal operating cycle from the date of Balance Sheet, it will be called 'Current Liability'. Operating cycle of a company may be a period of 12 months or more.

Operating Cycle : As per Schedule III : "An operating cycle is the time between the acquisition of assets for processing and their realization in cash or cash equivalents. Where the normal operating cycle cannot be identified, it is assumed to have a duration of 12 months".

For example, in a manufacturing concern oeprating cycle will be the time taken to purchase raw material, its processing into finished goods, selling it and its conversion into cash and cash equivalents :


Cash
Inventory of Raw Material (Inventory held for 2 months)
Inventory of work-in-progress (Production process 1.5 months)
Inventory of Finished goods (Inventory held for 3 months)
Trade Receivables (Credit Period allowed 2 months)

Hence, Operating Cycle = 2 months + 1.5 months + 3 months + 2 months
= 8.5 months

In case operating cycle cannot be identified, it is assumed to have a duration of 12 months from the date of Balance Sheet.

If the operating cycle is of a period more than 12 months (say 15 months), all liabilities of that business which are due for settlement within 15 months of the Balance Sheet date, shall be classified as Current Liabilities.

If the operating cycle is of a period less than 12 months (say 8 months), all liabilities of that business which are due for settlement within 12 months of the Balance Sheet date, shall be classified as Current Liabilities.

ILLUSTRATION 5.

Operating Cycle and the period when payment is made is given below. How will you classify the liability?

Particulars	*(i)*	*(ii)*	*(iii)*	*(iv)*	*(v)*	*(vi)*	*(vii)*
Operating Cycle (Months)	9	10	10	15	15	15	16
Expected period of payment of Trade Payables (Months)	10	12	14	12	13	18	15

SOLUTION :

While classifying the liabilities into Current and Non-Current following two points should be taken into consideration :

1. All liabilities, of which the payment is expected to made within 12 months from the date of Balance Sheet, shall be treated as Current. Period of operating cycle is irrelevant in such cases. Hence, trade payables in case of (*i*), (*ii*) and (*iv*) shall be treated as Current Liabilities.
2. Liabilities, of which the payment is expected to be made beyond 12 months from the date of Balance Sheet :
   (*i*) If payment period is less than the period of operating cycle, the liability shall be treated as current liability.
   Hence, trade payables in case of (*v*) and (*vii*) shall be treated as Current Liabilities.

(*ii*) If payment period is more than the period of operating cycle, the liability shall be treated as non-current liability.
Hence, trade payables in case of (*iii*) and (*vi*) shall be treated as Non-Current Liabilities.

Hence, the liabilities which are not classified as Current shall be classified as Non-Current Liabilities.

Current Liabilities :

Schedule III prescribes that Current Liabilities shall be classified as follows :

(A) **Short-term borrowings** : Borrowings which are due for payment within 12 months from the date of loan are termed Short-term Borrowings.
Short-term borrowings shall be classified as :

(*a*) Loans repayable on demand *i.e.* **Overdraft or Cash Credit from Banks.**

(*b*) Loans from other parties.

(*c*) Deposits.

(*d*) Other loans and advances (specify nature).

(B) **Trade Payables**
A payable shall be classified as a 'trade payable' if it is in respect of the amount due on account of goods purchased or services received in the normal course of business. It includes both 'Sundry Creditors' and Bills Payables'.

(C) **Other Current Liabilities** : All Current liabilities that are not short-term borrowings or trade payables.
The amounts shall be classified as :

(*a*) Current maturities of long-term debt;
Amount due to be paid within 12 months of the date of Balance Sheet out of long-term borrowings is shown as current maturities of long term debts such as debentures redeemable within one year.

(*b*) Interest accrued but not due on borrowings;

(*c*) Interest accrued and due on borrowings;

For example, if a Company pays interest on its debentures half-yearly on 30th June and 31st December, and assuming that the Company prepares its accounts on 31st March, 2020, and if the interest due on these debentures upto 31st December, 2019 remains unpaid on 31st March, 2020, it will be called 'Interest accrued and due'. Interest on the above debentures from 1st January 2020 to 31st March, 2020 will be termed 'Interest accrued but not due'.

(*d*) Income received in advance;

(*e*) **Unpaid dividends** : Dividends paid but they remain unclaimed by shareholders.

(*f*) Excess application money which is due for refund and interest accrued thereon is shown under 'Other Current Liabilities'.**

(*g*) Unpaid matured deposits and interest accrued thereon.**

(*h*) Unpaid matured debentures and interest accrued thereon.**

(*i*) Other payables (such as Outstanding Expenses, Calls in advance and interest thereon, Unclaimed dividends, Provident Fund Payable, GST Payable etc.)

(D) **Short-term Provisions**

Short-term Provisions are the provisions against which liability is likely to arise within 12 months from the date of Balance Sheet.

The amounts shall be classified as :

(*a*) Provision for employee benefits (who will retire within 12 months from the date of Balance Sheet.)**

(*b*) Provision for Tax

(*c*) Provision for Expenses

(*d*) Provision for Discount on Debtors

(*e*) Other Provisions**

Attention :

There is a distinction between a liability and a provision. If an amount is payable in future and the figure is exact, it is a liability. For instance, if the salary for the month of March totalling ₹2,00,000 is outstanding on 31st March, such amount of outstanding salary is a definite liability. If the amount of a liability is not certain, it will be a provision such as provision for taxation etc.

There is distinction between 'Reserves' and 'Provisions'. Reserves mean accumulated profits and it is created to strengthen the financial position of the Company and to meet unforeseen (unknown) liabilities and losses.

'Provision' is an amount provided for any known liability whose amount as yet is uncertain. Provision is made to meet a specific liability of which the amount cannot be determined with substantial accuracy. Provision is also made for known losses such as 'Provision for Depreciation'.

Explanation of Assets

(1) **Non-Current Assets :** These assets are classified into five major heads :

(A) **Fixed Assets :** Fixed assets refer to those assets which are held for continued use in the business for the purpose of producing goods or services and are not meant for sale. They are categorised into :

(*i*) **Tangible Assets :** Tangible assets are the assets which can be physically seen and touched.

Classification shall be given as :

- (*a*) Land
- (*b*) Buildings
- (*c*) Plant and Equipment
- (*d*) Furniture and Fixtures
- (*e*) Vehicles
- (*f*) Office equipment.
- (*g*) Others (specify nature).

It is necessary to give the following information regarding each class or kind of fixed tangible asset :

- (*a*) Original cost
- (*b*) Addition (purchase)
- (*c*) Deductions (sale)
- (*d*) Total depreciation written off or provided for up to the end of the year.

(*ii*) **Intangible Assets** : Intangible assets are the assets which do not have a physical existence and thus, cannot be seen or touched.

Classification shall be given as :

- (*a*) Goodwill.
- (*b*) Brands/trademarks.
- (*c*) Computer software** and Mining rights.**
- (*d*) Mastheads and publishing titles.**
  (Masthead refers to the name of a newspaper or magazine printed at the top of the first page)
- (*e*) Copyrights and patents.
- (*f*) Recipes, formulae, models and designs.**
- (*g*) Licenses and franchise.**

(However students need to know under which heading / sub-heading the items marked above appear in Schedule III)**

It may be mentioned that the term 'Depreciation' is used for writing off fixed tangible assets over their useful life whereas the term 'amortisation' is used for writing off fixed intangible assets over their useful life.

(*iii*) **Capital Work-in-Progress**** : It refers to fixed tangible assets which are under construction such as Building, Plant & Equipment etc. **(Students need to know only the meaning and under which heading / sub-heading the items appear in Schedule III).**

(*iv*) **Intangible Assets under Development**** : Like patents, intellectual property rights etc. which are being developed by the Company. **(Students need to know only the meaning and under which heading / sub-heading the items appear in Schedule III).**

(B) **Non-current investments** (investments for more than one year) : Non-Current Investments are those investments which are held by a Company not with the purpose of selling but to retain them.

Non-current investments shall be classified as trade investments and other investments :

Trade Investments refer to the investments made by a Company in shares or debentures of another company, not being its subsidiary, to promote its own trade and business.

Other Investments are the investments which are not trade investments.
Investments in property**
In equity shares**
In preference shares**
In debentures**
In mutual funds**
In partnership firms**
In Govt. securities**
(However, students need to know the heading / sub-heading under which the items marked ** above appear in Schedule III)

(C) **Deferred Tax Assets (Net)** : (Students need to know only its meaning and under which heading / sub-heading this item appear in Schedule III)**

A deferred tax asset comes into force when accounting income is less than taxable income.

(D) **Long-term loans and advances**

These are the loans and advances which are expected to be received back in cash or kind after more than 12 months from the date of Balance Sheet. They are classified as :

(*a*) **Capital Advances;**
Advances given for acquiring fixed assets are called 'Capital Advances'. These advances are not received back in cash but are received in the form of some fixed asset. Since they are ultimately converted into the fixed assets of the company, they are classified as long-term advances.

(*b*) **Security Deposits;**
Security deposits that are given for a period of more than 12 months from the date of Balance Sheet are classified into 'Long-term Advances. Examples are security deposit for electricity and telephone etc.

(*c*) **Other Loans and Advances**

- Long term Loans to Employees
- Long term Advances to Suppliers

(E) **Other non-current assets****

(*i*) Long term Trade Receivables**

(*ii*) **Others** : Such as Insurance Claims receivable and unamortized expenses to be written off after 12 months from the date of Balance Sheet or after the period of operating cycle, whichever is later.

(2) Current Assets :

An asset shall be classified as current when it satisfies any of the following criteria :

(*a*) it is expected to be realised in, or is intended for sale or consumption in the company's normal operating cycle; or

(*b*) it is held primarily for the purpose of being traded; or

(*c*) it is expected to be realised within twelve months after the reporting date, *i.e.* Balance Sheet date

(*d*) it is cash or cash equivalent.

All other assets shall be classified as non-current.

Operating Cycle : An operating cycle is the time between the acquisition of assets for processing and their realisation in cash or cash equivalents. Where the normal operating cycle cannot be identified, it is assumed to have a duration of 12 months.

If the operating cycle of a business is of a period of more than 12 months (say 18 months), all assets of that business that are expected to be consumed or realised within 18 months of the Balance Sheet date shall be classified as Current Assets.

If the operating cycle is of a period of less than 12 months (say 10 months), all assets of that business that are expected to be consumed or realised within 12 months of the Balance Sheet date, shall be classified as Current Assets.

ILLUSTRATION 6.

Operating Cycle and the expected period of realisation of trade receivables is given below. How will you classify the asset?

Particulars	(i)	(ii)	(iii)	(iv)	(v)	(vi)	(vii)
Operating Cycle (Months)	9	17	10	10	14	24	10
Expected period of realisation of trade receivables (Months)	8	15	11	15	16	20	12

SOLUTION :

1. All assets, that are expected to be realised within 12 months from the date of Balance Sheet, shall be treated as Current. Period of operating cycle is irrelevant in such cases. Hence, trade receivables in case of (i), (iii) and (vii) shall be treated as current assets.

2. Assets, that are expected to be realised in more than 12 months from the date of Balance Sheet :

   (*i*) If the period of realisation of asset is less than the period of operating cycle, the asset shall be treated as Current Asset. Hence, trade receivables in case of (ii) and (vi) shall be treated as Current Assets.

   (*ii*) If the period of realisation of asset is more than the period of operating cycle, the asset shall be treated as Non-Current Asset. Hence, trade receivables in case of (iv) and (v) shall be treated as Non-Current Assets.

Current Assets are classified in the following six heads :

(A) **Current Investments** : Current Investments are those investments which are held to be converted into cash within a short period i.e. within 12 months from the date of their purchase. They are classified into :

(*a*) Investments in Partnership firms.**

(*b*) Investments in Equity Shares;**

(*c*) Investment in Preference Shares;**

(*d*) Investments in Government or trust securities;**

(*e*) Investments in Debentures or bonds;**

(*f*) Investments in Mutual Funds etc.**

- Short Term Investment (to be taken as cash equivalent while preparing Cash Flow Statement).
- Marketable Securities (to be taken as cash equivalent while preparing Cash Flow Statement).

(B) **Inventories** : Inventories means stock held for the purpose of trade in the normal course of business, *i.e.*, for manufacturing or trading of goods.

Inventories include the following :

(*a*) Raw materials;

(*b*) Work-in-progress;

(*c*) Finished goods;

(*d*) Stock-in-trade (in respect of goods acquired for trading);

(*e*) Stores and spares;

(*f*) Loose tools.

(*g*) Goods in Transit**

(C) **Trade Receivables** : Trade receivables refer to the amount receivable on account of sale of goods or services rendered by the company in the normal course of business. They are classified as current assets if the amount is expected to be realised within a period of 12 months from the date of Balance Sheet or within the operating cycle of the business.

Trade Receivables include both Debtors and Bills Receivables.

Debtors :
Less : Provision for Doubtful Debts
Less : Provision for Discount on Debtors

(D) **Cash and Bank Balance**

(*i*) Cash and Bank Balance shall be classified as :

(*a*) Balances with Banks in Current accounts.

(*b*) Balances with Banks in Deposit accounts with original maturity less than 3 months.

(*c*) Cheques, Drafts on Hand;

(*d*) Cash on Hand

(*ii*) Other Bank Balances :

(*a*) Earmarked bank balances (for example, for unpaid dividend)

(*b*) Short term bank deposits (upto maturity of 12 months)

(E) **Short-term loans and advances :** Expected to be realised within 12 months from the Balance Sheet date or within the Operating Cycle, if the Operating Cycle is of more than 12 months.

(*i*) Loans and Advances to related parties.

(*ii*) Others

(F) **Other current assets** (specify nature).
This is an all-inclusive heading, which incorporates current assets that do not fit into any other asset categories such as prepaid expenses, dividend receivable, interest accrued on investments and advance tax.

Explanation of contingent liabilities and Capital commitments (to the extent not provided for)

1. **Contingent Liabilities** : These liabilities refer to the claims which are uncertain to arise because they are dependent on a happening in future. They are not recorded in the books of accounts **but disclosed in the Notes to Accounts.**

Contingent liabilities shall be classified as :

(*a*) Claims against the company not acknowledged as debt;

(*b*) Liabilities for Bills discounted;

(*c*) Proposed Dividend for Current Year;

(*d*) Guarantees given by the Company;

2. **Capital Commitments** : A future liability for capital expenditure in respect of which contracts have been made.

(*a*) Uncalled amount on partly paid shares;
If the Company holds partly-paid shares of other Companies as investment, the uncalled amount on these shares is a commitment, as it will have to be paid when called.

(*b*) Estimated amount of capital contracts remaining to be executed and not provided for (penalty).

(*c*) Other commitments (specify nature) such as arrears of dividends on Cumulative Preference Shares.

Preparation of Part II Schedule III

PART II

FORMAT OF STATEMENT OF PROFIT AND LOSS

IMPORTANT NOTE

Preparation of Part II of Schedule III is excluded from the scope of syllabu

However, for the preparation of the Comparative and Common Size Income Statement (Section B – Unit 4 in the scope of syllabus), the extent and format of the Statement of Profit and Loss has been modified. The modified version of the Statement of Profit and Loss is as follows :

Name of the Company ....
Profit and loss statement for the year ended ....

(₹ in ....)

	Particulars	*Note No.*	*Figures for the current reporting period*	*Figures for the previous reporting period*
I.	Revenue from operations		xxx	xxx
II.	Other Income		xxx	xxx
III.	Total Revenue (I + II)		xxx	xxx
IV.	Expenses :			
	Cost of materials consumed		xxx	xxx
	Purchases of Stock-in-Trade		xxx	xxx
	Changes in inventories of finished goods, work-in-progress and Stock-in-Trade		xxx	xxx
	Employee benefits expenses			
	Finance costs			
	Depreciation and amortization expenses			
	Other expenses			
	Total expenses		xxx	xxx
V.	Profit before Tax (III–IV)		xxx	xxx
VI.	*Less* : Tax		(xxx)	(xxx)
VII.	Profit after Tax (V–VI)		xxx	xxx

Notes : General Instructions for Preparation of Statement of Profit and Loss

Revenue from Operations : It is the revenue earned from business operations. For example :

- Net Sales
- Sale of scrap
- Revenue from services

Other Income : Other income is the revenue that is not earned from business operations. It shall be classified as :

- Rent received
- Interest and Dividend Received
- Profit from Sale of Fixed Assets/Investments

Cost of Materials Consumed

- Opening Stock of Materials + Net Purchases – Closing Stock of Materials

Purchase of Stock-in-Trade

- Net Purchases

Changes in Inventories of Finished Goods, Work-in-Progress and Stock-in-Trade

- Opening Stock – Closing Stock

Employee Benefit Expenses

- Wages
- Salaries
- Staff Welfare Expenses such as canteen expenses
- Contribution to Provident Fund and other staff welfare funds.**

Depreciation and Amortisation Expenses

Finance Costs

- Amount of interest paid by the company on its borrowings

Other Expenses

Includes expenses other than the above six heads of expenses. These could be :

- Telephone expenses
- Rent and Taxes
- Selling and Distribution Expenses
- Advertisement Expenses
- Loss on Sale of Fixed Assets / Investments
- Cash Discount allowed
- Bad Debts
- Provision for Bad and Doubtful Debts.

EXAMINATION NOTES

Above mentioned classification of liabilities and assets may be summarised as follows :

- **NON-CURRENT LIABILITIES** shall include the liabilities due after one year. It shall include the following :
- **Long-term Borrowings** : Such as Debentures and Bonds issued by the Company, Premium on Redemption of Debentures, Term Loan from Bank, Loan from other parties, Public Deposits (Unless specified, it will be assumed that deposits are for more than one year).
- **Deferred Tax Liabilities.**
- **Long-term Provisions** : Such as Provision for Employee Benefits, Provision for Provident Fund, Provision for Warranties.

CURRENT LIABILITIES shall include the liabilities due within one year. It shall include the following :

- **Short-term Borrowings :** Such as Bank Overdraft, Cash Credit.
- **Trade Payables** : Sundry creditors and Bills Payable will be termed Trade Payables.

- **Other Current Liabilities** : Such as
  - (*i*) Current Maturities of Long-term Debts.
  - (*ii*) Interest accrued but not due on borrowings;
  - (*iii*) Interest accrued and due on borrowings;
  - (*iv*) Income received in advance;
  - (*v*) Unpaid dividends; Unclaimed Dividends;
  - (*vi*) Outstanding expenses;
  - (*vii*) Calls in advance and interest accrued thereon.
  - (*viii*) Provident Fund Payable
- **Short-term Provisions** : Such as
  - (*i*) Provision for Employee Benefits
  - (*ii*) Provision for Tax;

NON-CURRENT ASSETS shall include the assets held for more than one year. It shall include the following :

- **Fixed Assets**
  - (*i*) **Tangible Assets** : Such as Land, Buildings, Plant, Furniture & Fixtures, Live Stock, Computers, Vehicles, Office Equipments, etc.
  - (*ii*) **Intangible Assets** : Such as Goodwill, Patents, Computer Software, etc.
  - (*iii*) Capital work in Progress
  - (*iv*) Intangible Assets under Development
- **Non-Current Investments** (Unless specified, it will be assumed that Investments are for more than one year) : Such as
  - (*i*) Investment in Equity Shares;
  - (*ii*) Investment in Preference Shares;
  - (*iii*) Investment in Govt. or Trust Securities;
  - (*iv*) Investment in Debentures or Bonds;
  - (*v*) Investment in Mutual Funds.
- **Deferred Tax Assets**
- **Long-term Loans and Advances** : Such as Security Deposit with Electricity Co.

CURRENT ASSETS shall include the assets held for one year or less. It shall include the following :

- **Current Investments** : Short-term Investments
- **Inventories** : Raw Materials, Work in Progress, Finished Goods, Stock in Trade, Loose Tools, Goods in Transit etc. will be termed Inventories.
- **Trade Receivables** : Sundry Debtors and Bills Receivable will be termed Trade Receivables. Provision for Doubtful Debts will be deducted from Trade Receivables.

- **Cash and Bank Balance**
- **Short-term Loans and Advances** : Such as Advances recoverable in cash
- **Other Current Assets** : Such as Prepaid Exp., Dividend Receivable, accrued income, Advance Tax.

Contingent Liabilities and Commitments shall include the following :

- **Contingent Liabilities :**
  - (*i*) Claims against the company not acknowledged as debts.
  - (*ii*) Bills Discounted but not matured.
  - (*iii*) Proposed Dividend for Current Year
  - (*iv*) Guarantees given by the Company.
- **Commitments :**
  - (*i*) Contracts remaining to be executed.
  - (*ii*) Uncalled liability on partly paid shares;
  - (*iii*) Arrears of dividends on cumulative preference shares.

Some special items related to Balance Sheet :

(*i*) **Calls in Arrears** : This item usually appears on the debit side of the Trial Balance and represents the amount not paid by the shareholders on the calls made by the Company. This is shown on the equity and liabilities side as a deduction from 'Subscribed but not fully paid' capital.

(*ii*) **Calls-in-Advance** : This is shown separately in the Balance Sheet under the heading 'Other Current Liabilities'.

(*iii*) **Forfeited Shares Account** : This item appears on the credit side of the Trial Balance and is recorded on the equity and liability side by adding to the subscribed capital.

(*iv*) **Securities Premium Reserve** : This is recorded on the equity and liability side under the heading 'Reserves and Surplus'.

Explanation of Some Specific Terms

Capital Structure

The term 'Capital Structure' refers to the proportion between the various long-term sources of finance in the total capital of the firm. The major sources of long-term finance include 'Proprietor's Funds' and 'Borrowed Funds'. Proprietor's Funds include equity capital, preference capital, reserves and surpluses (*i.e.*, retained earnings) and Borrowed Funds include long-term debts such as loans from financial institutions, debentures etc. In the capital structure decisions, it is determined as to what should be the proportion of each of the above sources of finance in the total capital of the firm.

Distinction between Tangible and Intangible Assets :

Tangible assets are those assets which can be seen and touched. In other words, which have a physical existence such as Land, Building, Plant, Furniture, Stock, Cash etc.

Intangible assets are those assets which do not have a physical existence and which cannot be seen or felt. Examples of such assets are Goodwill, Patents, Trade Marks and Prepaid Expenses. Intangible assets are also valuable assets. For example, with the help of Patents (know-how) businessman is able to produce goods and then his goodwill helps in attracting customers easily. Therefore the intangible assets help the firm in earning profits as much as the tangible assets. Hence, both tangible and intangible are valuable assets. Value of intangible assets is based on the benefit and facility available to the business from such assets.

Provisions :

According to the Companies Act the term 'Provision' refers to any of the following amounts :—

(*a*) The amount written off or retained by way of providing for depreciation, renewals or diminution in value of assets; or

(*b*) The amount retained by way of providing for any known liability of which the amount cannot be determined with substantial accuracy.

It should be clearly understood that if the amount of a known liability can be determined with reasonable accuracy, it must be classified as an outright liability and not a provision. Also if any excess provision is made knowingly or intentionally, the amount in excess of the actual need will be treated as 'reserve'.

Examples of Provisions :

1. Provision for Depreciation of Assets.
2. Provision for Taxation.
3. Provision for Bad and Doubtful Debts.
4. Provision for Discount on Debtors.
5. Provision for Repairs and Renewals of assets.

Reserves :

Reserves mean amounts set aside out of profits and other surpluses to meet future uncertainties. In other words, a reserve is meant for meeting any unknown liability or loss in the future. According to William Pickles, "Reserves mean the amounts set aside out of profits and other surpluses, which are not earmarked in any way to meet any particular liability, known to exist on the date of the Balance Sheet".

Examples of reserves are : (1) General Reserve, (2) Capital Reserve, (3) Dividend Equalisation Reserve, (4) Investment Fluctuation Fund, (5) Workmen Compensation Reserve, (6) Reserve for Redemption of Debentures.

Distinction between Provision and Reserve

Basis of Distinction		Provision	Reserve
1.	**Meaning**	It is created to meet a known liability.	It is created to meet an unknown liability.
2.	**Necessity**	Creation of provision is a legal necessity. Provisions have to be provided for even if there are no profits.	Creation of reserves is discretionary. It can be created only if adequate profits have been earned.

3	Object	The object is to provide for depreciation, doubtful debts and other specific liabilities.	The object of reserves is to strengthen the financial position of the business.
4	Mode of Creation	It is created by debiting to P & L statement. Hence, net profit cannot be calculated unless all provisions have been debited to P & L statement.	It is created not by debiting to P & L statement but through deduction from 'Surplus'. As such, it is created after the calculation of net profit.
5	Investment outside the business.	Provisions are never invested outside the business.	Reserves may be invested outside the business.
6	Presentation in Balance Sheet.	It is either shown on the assets side by way of deduction from the asset for which it is created or as a liability item on the liabilities side.	It is shown on the liabilities side under the head 'Reserves and Surplus'.
7	Utilisation for dividends.	It cannot be utilised for distribution as dividends among shareholders.	It can be utilised for distribution as dividends among shareholders.
8	Utilisation for other purposes.	It is created to provide for a specific loss and hence can only be used for meeting that loss.	It is not created to provide for a specific loss and hence can be used for any purpose.

Types of Reserves

(A) **Revenue Reserves** — These reserves come into existence out of profits which have been earned in the course of day-to-day business operations. Therefore, the revenue reserves represent undistributed profits and as such are available for the distribution of dividends.

Revenue reserves may be of the following two types :—

(*i*) **General Reserve** — Usually, the businessmen do not withdraw the entire profits from the business but retain a part of it in the business to meet unforeseen future uncertainties. Profits so retained in the business for 'a rainy day' are known as 'General Reserve'. Similarly, Companies also do not distribute the entire profits as dividends but keep aside a part of it in the form of General Reserve. Such reserves are also termed as 'Contingency Reserves' or 'Free Reserves' because these are not created for any specific purpose and can be freely used for any purpose.

(*ii*) **Specific Reserve** — Such a reserve is created for a specific purpose and can be utilised only for that purpose. Examples of specific reserves are :—

(I) Dividend Equalisation Reserve

(II) Reserve for Replacement of Asset

(III) Investment Fluctuation Fund

(IV) Workmen Compensation Reserve

(V) Debenture Redemption Reserve

(B) **Capital Reserves :—** In addition to the normal profits, capital profits are also earned in the business from many sources. The reserves created out of such capital profits are known as Capital Reserves. Such reserves generally, are not available for distribution as cash dividend among the shareholders of a Company. Profits received from the following sources are termed as capital profits :—

1. Profits on the sale of fixed assets.
2. Profits on the revaluation of fixed assets and liabilities.
3. Premiums received on issue of Shares or Debentures.
4. Profit on the purchase of a running business.
5. Profit prior to the incorporation of a Company.
6. Profit from the reissue of forfeited shares.
7. Profit on redemption of debentures.

Distinction between Revenue Reserves and Capital Reserves

	Basis of Distinction	*Revenue Reserves*	*Capital Reserves*
1.	**Source of Creation**	These reserves are created out of revenue profits which arise from the normal operating activities of the business and are otherwise available for disribution of dividends.	These reserves are created out of capital profits, which do not arise from the normal operating activities of the business and are not available for distribution of dividends.
2.	**Usage**	A specific reserve can be utilised only for the earmarked purpose while a general reserve can be utilised for any purpose including distribution of dividends to shareholders without any pre-conditions.	Normally, these reserves cannot be utilised for distribution of dividends to shareholders. However, some capital reserves can be utilised to distribute dividends subject to fulfilment of certain conditions laid down by Companies Act.
3.	**Purpose**	These reserves are created for meeting unforeseen losses and for strengthening the financial position of business.	These reserves are created to meet Capital losses or may be used for purposes laid down by Companies Act.

ILLUSTRATION 7.

Name the major headings under which the equity & liabilities side of a Company's Balance Sheet is organised and presented. *(From I.S.C. Guidelines, 2013)*

SOLUTION :

The major headings on the Equity & Liabilities side are :

I. Shareholder's Funds
II. Share Application money pending allotment
III. Non-Current Liabilities
IV. Current Liabilities

ILLUSTRATION 8.

Name the major headings under which the assets side of a Company's Balance Sheet is organised and presented.

SOLUTION :

The major headings on the assets side are :

I. Non-Current Assets
II. Current Assets

ILLUSTRATION 9.

Name the Sub-headings under which Shareholder's Funds shall be classified in a Company's Balance Sheet. *(From I.S.C. Guidelines, 2013)*

SOLUTION :

Shareholder's funds shall be classified as follows :

(*a*) Share Capital
(*b*) Reserves and Surplus
(*c*) Money received against share warrants.

ILLUSTRATION 10.

Name the Sub-headings under which Non-Current Liabilities shall be classified in a Company's Balance Sheet.

SOLUTION :

Non-Current Liabilities shall be classified as follows :

(*a*) Long-term borrowings
(*b*) Deferred tax liabilities
(*c*) Other Long-term liabilities
(*d*) Long-term provisions.

ILLUSTRATION 11.

Name the Sub-headings under which Non-Current Assets shall be classified in a Company's Balance Sheet.

SOLUTION :

Non-Current Assets shall be classified as follows :

(*a*) Fixed Assets
(*b*) Non-Current Investments
(*c*) Deferred tax assets
(*d*) Long-term loans and advances
(*e*) Other non-current assets

ILLUSTRATION 12.

Under what heads the following items on the Equity & Liabilities side of the Balance Sheet of a Company will be presented :

(*i*) Proposed Dividend
(*ii*) Unpaid/Unclaimed Dividend *(C.B.S.E. 2020)*

(*iii*) Debentures Issued by the Company *(C.B.S.E. 2020)*
(*iv*) Matured Debentures
(*v*) Calls in Arrears *(C.B.S.E. 2020)*
(*vi*) Sinking Fund
(*vii*) Provision for Provident Fund
(*viii*) Bills Payable
(*ix*) Public Deposits

SOLUTION :

Items	*Heading*	*Sub-heading (if any)*
(*i*) Proposed Dividend	Contingent Liabilities (to be shown in notes to accounts).	
(*ii*) Unpaid/Unclaimed Dividend	Current Liabilities	Other Current Liabilities
(*iii*) Debentures Issued by the Company	Non-Current Liabilities	Long-term Borrowings
(*iv*) Matured Debentures	Current Liabilities	Other Current Liabilities
(*v*) Calls in Arrears	Shareholder's Funds	It will be deducted from 'Subscribed but not fully paid Capital'
(*vi*) Sinking Fund	Shareholder's Funds	Reserves and Surplus
(*vii*) Provision for Provident Fund	Non-Current Liabilities	'Long-term Provisions'
(*viii*) Bills Payable	Current Liabilities	Trade Payables
(*ix*) Public Deposits	Non-Current Liabilities	Long term Borrowings

Attention : Sundry Debtors and Bills Receivables will be termed 'Trade Receivables'.

Sundry Creditors and Bills Payables will be termed 'Trade Payables'.

ILLUSTRATION 13.

Under what heads the following items on the Assets side of the Balance Sheet of a Company will be presented :

(*i*) Sundry Debtors *(I.S.C. 2020)*
(*ii*) Patents and Trade Marks *(I.S.C. 2020)*
(*iii*) Shares in DCM Limited
(*iv*) Bills Receivable
(*v*) Advances recoverable in cash within the operating cycle
(*vi*) Prepaid Insurance *(C.B.S.E. 2019)*
(*vii*) Work-in Progress
(*viii*) Finished Goods *(I.S.C. 2020)*

SOLUTION :

Items	*Heading*	*Sub-heading (if any)*
(*i*) Sundry Debtors	Current Assets	Trade Receivables

(*ii*) Patents and Trade Marks	Non-Current Assets	Fixed Assets — Intangible Assets
(*iii*) Shares in DCM Ltd.	Non-Current Assets	Non-Current Investments
(*iv*) Bills Receivable	Current Assets	Trade Receivables
(*v*) Advances Recoverable in Cash within the Operating Cycle	Current Assets	'Short-term Loans and Advances'
(*vi*) Prepaid Insurance	Current Assets	'Other Current Assets'
(*vii*) Work-in-Progress	Current Assets	'Inventories'
(*viii*) Finished Goods	Current Assets	'Inventories'

ILLUSTRATION 14.

Under what headings will you show the following items in the Balance Sheet of the Company. *(C.B.S.E. 2020)*

(*i*) Goodwill
(*ii*) Unclaimed Dividends
(*iii*) Provision for Tax
(*iv*) Securities Premium Reserve
(*v*) Loose Tools *(C.B.S.E. 2020)*
(*vi*) Arrears of Fixed Cumulative Dividends
(*vii*) Preliminary Expenses

SOLUTION :

Items	*Heading*	*Sub-heading (if any)*
(*i*) Goodwill	Non-Current Assets	Fixed Assets — Intangible Assets
(*ii*) Unclaimed Dividends	Current Liabilities	Other Current Liabilities
(*iii*) Provision for Tax	Current Liabilities	Short-term Provisions
(*iv*) Securities Premium Reserve	Shareholder's Funds	Reserve and Surplus
(*v*) Loose Tools	Current Assets	Inventories
(*vi*) Arrears of Fixed Cumulative Dividends	Commitments (to be shown in notes to Accounts)	
(*vii*) Preliminary Expenses	These expenses are to be written off from Securities Premium Reserve or from General Reserve or from Surplus in the year in which they occur.	

ILLUSTRATION 15.

Under what headings will you show the following items?

(*a*) Interest Accrued and due on Unsecured Loan.
(*b*) Interest Accrued and due on Secured Loan.
(*c*) Interest Accrued but not due on Loan.

(*d*) Mortgage Loan
(*e*) Government and Trust Securities
(*f*) Uncalled liability on partly paid shares
(*g*) Deposits with Customs and Electricity Supply Company.
(*h*) General Reserve
(*i*) Capital Reserve

SOLUTION :

Items	*Heading*	*Sub-heading (if any)*
(*a*) Interest Accrued and due on Unsecured Loan	Current Liabilities	Other Current Liabilities
(*b*) Interest Accrued and due on Secured Loan	Current Liabilities	Other Current Liabilities
(*c*) Interest Accrued but not due on Loan	Current Liabilties	Other Current Liabilities
(*d*) Mortgage Loan	Non-Current Liabilities	Long term Borrowings
(*e*) Government and Trust Securities	Non-Current Assets	Non-Current Investments
(*f*) Uncalled liability on Partly-paid shares	Commitments (to be shown in notes to accounts)	
(*g*) Deposits with Customs and Electricity Supply Company	Non-Current Assets	'Long-term Loans and Advances'
(*h*) General Reserve	Shareholder's Funds	Reserves and Surplus
(*i*) Subsidy Reserve	Shareholder's Funds	Reserves and Surplus

ILLUSTRATION 16.

How would you disclose the following items in the Balance Sheet of a Company :

(*i*) Premium on Redemption of Debentures
(*ii*) Debit balance of Statement of Profit & Loss
(*iii*) Term Loan from Bank *(C.B.S.E. 2018)*
(*iv*) Loan repayable on demand
(*v*) Shares in S.B.I.
(*vi*) Investments in Debentures
(*vii*) Interest Accrued on Investments
(*viii*) Guarantees given by the Company

SOLUTION :

S. No.	*Item*	*Major Head*	*Sub-head*
(*i*)	Premium on Redemption of Debentures.	Non Current Liabilities	Long term Borrowings

(*ii*)	Debit balance of Statement of Profit & Loss.	Shareholder's Funds	Reserve and Surplus (shown as a negative figure) under 'Surplus'.
(*iii*)	Term Loan from Bank	Non Current Liabilities	Long term Borrowings
(*iv*)	Loan repayable on demand	Current Liabilities	Short term Borrowings
(*v*)	Shares in S.B.I.	Non Current Assets	Non Current Investments
(*vi*)	Investments in Debentures	Non Current Assets	Non Current Investments
(*vii*)	Interest Accrued on Investments	Current Assets	Other Current Assets
(*viii*)	Guarantees given by the Company.	Contingent Liability (to be shown in 'Notes to Accounts')	

ILLUSTRATION 17.

How will you show the following items in the Balance Sheet of a Company.

(*i*) Provision for Doubtful Debts

(*ii*) Money Received against share warrants

(*iii*) Cheques/Drafts in hand *(C.B.S.E. 2018)*

(*iv*) Bank Overdraft *(C.B.S.E. 2020)*

(*v*) Deferred Tax Liabilities

(*vi*) Deferred Tax Assets

(*vii*) Computer

(*viii*) Computer Software *(C.B.S.E. 2020)*

(*ix*) Building

(*x*) Building under construction

SOLUTION :

S. No.	*Item*	*Major Head*	*Sub Head*
(*i*)	Provision for Doubtful Debts	Current Assets	Deducted from Trade Receivables
(*ii*)	Money Received against share warrants	Shareholder's Funds	—
(*iii*)	Cheques/Drafts in hand	Current Assets	Cash and Bank Balance
(*iv*)	Bank Overdraft	Current Liabilities	Short term Borrowings
(*v*)	Deferred Tax Liabilities	Non Current Liabilities	Deferred Tax Liabilities
(*vi*)	Deferred Tax Assets	Non Current Assets	Deferred Tax Assets
(*vii*)	Computer	Non Current Assets	Fixed Assets – Tangible Assets

(*viii*) Computer Software	Non Current Assets	Fixed Assets – Intangible Assets
(*ix*) Building	Non Current Assets	Fixed Assets – Tangible Assets
(*x*) Building under Construction	Non Current Assets	Fixed Assets – Capital Work in progress

ILLUSTRATION 18.

From the list of following assets and liabilities, prepare the Balance Sheet of the Company as per Schedule III, Part I of the Companies Act 2013 :

Nishant Co. Ltd.

Liabilities		*Amount*	*Assets*		*Amount*
		₹			₹
Sundry Creditors		1,00,000	Cash at Bank		79,800
Securities Premium		50,000	Cash in Hand		1,500
Interest Accrued and Due			Investments		95,000
on Debentures		28,000	Preliminary expenses		9,000
Authorised Share Capital			Loans and advances to staff		95,000
1,20,000 shares of			Goodwill		50,000
₹10 per share		12,00,000	Buildings		6,00,000
Subscribed Capital 80,000			Plant and Machinery	6,60,000	
shares of ₹10 each	8,00,000		*Less :* Depreciation	66,000	5,94,000
Less : Calls in arrears			Inventories		10,000
(₹3 per share on			Debtors	1,74,000	
5,000 shares)	15,000	7,85,000	*Less :* Provision for		
Statement of Profit and Loss			Doubtful Debts	8,700	,65,300
Balance		75,000	Furniture		114,400
6% Debentures		6,00,000			
Bills Payable		76,000			

SOLUTION :

Nishant Co. Ltd.

BALANCE SHEET *as at* ....

Particulars	*Note No.*	*Current year* ₹	*Previous year* ₹
I. EQUITY AND LIABILITIES :			
(1) Shareholders' funds			
(*a*) Share capital	1	7,85,000	
(*b*) Reserves and surplus	2	1,16,000	
(2) Share application money pending allotment			
(3) Non-Current Liabilities			
(*a*) Long-term Borrowings	3	6,00,000	
(*b*) Other Long-term Liabilities			
(*c*) Long-term Provisions			

(4) Current Liabilities			
(*a*) Short-term Borrowings			
(*b*) Trade payables	4	1,76,000	
(*c*) Other Current Liabilities	5	28,000	
(*d*) Short-term provisions		—	
TOTAL		17,05,000	
II. ASSETS			
(1) Non-Current Assets			
(*a*) Fixed Assets			
(*i*) Tangible Assets	6	12,08,400	
(*ii*) Intangible Assets	7	50,000	
(*b*) Non-current investments		95,000	
(*c*) Long-term Loans and Advances			
(*d*) Other Non-Current Assets			
(2) Current Assets			
(*a*) Current Investments			
(*b*) Inventories		10,000	
(*c*) Trade receivables	8	1,65,300	
(*d*) Cash and Bank Balance	9	81,300	
(*e*) Short-term Loans and Advances	10	95,000	
(*f*) Other Current Assets			
TOTAL		17,05,000	

Notes to Accounts :

		₹	₹
(1) **Share Capital :**			
Authorised .			
1,20,000 shares of ₹10 each			12,00,000
Issued :			
..... shares of ₹10 each			
Subscribed and Fully Paid Capital :			
75,000 Shares of ₹10 each		7,50,000	
Subscribed but not fully paid capital :			
5,000 Shares of ₹10 each	50,000		
Less : Calls in arrears	15,000	35,000	7,85,000
(2) **Reserves and Surplus :**			
Securities Premium	50,000		
Less : Preliminary Expenses Written off	9,000	41,000	
Surplus		75,000	1,16,000
(3) **Long term Borrowings :**			
6% Debentures			6,00,000
(4) **Trade Payables :**			
Bills Payable		76,000	

Sundry Creditors		1,00,000	1,76,000
(5) **Other Current Liabilities :**			
Interest Accrued and Due on Debentures			28,000
(6) **Tangible Assets :**			
Building		6,00,000	
Plant and Machinery	6,60,000		
Less : Depreciation	66,000	5,94,000	
Furniture		14,400	12,08,400
(7) **Intangible Assets :**			
Goodwill			50,000
(8) **Trade Receivables :**			
Debtors	1,74,000		
Less : Provision for Doubtful Debts	8,700		1,65,300
(9) **Cash and Bank Balance :**			
Cash at Bank		79,800	
Cash in Hand		1,500	81,300
(10) **Short term Loans and Advances :**			
Loan to Staff			95,000

ILLUSTRATION 19.

From the following balances extracted on 31st March 2022 from the books of Modern Ltd., prepare a Balance Sheet in the form prescribed under the Indian Companies Act 2013 :

	₹	₹
Land	80,000	
Cash in Mill	7,000	
Share Capital (₹10 each)		6,30,000
Building	2,12,500	
Calls in arrear (₹2.50 per share on 10,000 shares)	25,000	
Trade Payables		6,18,000
General Reserve		1,54,000
Preliminary Expenses	30,000	
Brokerage on shares	12,000	
Stores	90,000	
Wages due		29,000
Godown rent due		3,600
Stock in trade	2,50,000	
Unexpired Insurance	8,200	
Cash in office	1,25,000	
Employee Benefit Fund		15,000
Salaries due		3,500
Bad debts provision		6,500
Cash at Bank	62,000	

Live stock	4,900	
Machinery	5,08,000	
Loose Tools	1,30,000	
Trade Receivables	1,20,000	
Unclaimed dividends		5,000
Statement of Profit and Loss Balance		2,00,000
15% debentures		1,00,000
Bank loan account		1,50,000
Investments	2,50,000	
	19,14,600	19,14,600

Note : Bills discounted but not matured ₹40,000.

SOLUTION :

Modern Ltd.

BALANCE SHEET *as at 31st March, 2022*

Particulars	*Note No.*	*31.3.2022* ₹	*31.3.2021* ₹
I. EQUITY AND LIABILITIES			
(1) Shareholders' funds			
(*a*) Share capital	1	6,05,000	
(*b*) Reserves and surplus	2	3,12,000	
(2) Share application money pending allotment			
(3) Non-Current Liabilities			
(*a*) Long-term Borrowings	3	2,50,000	
(*b*) Other Long-term Liabilities			
(*c*) Long-term Provisions	4	15,000	
(4) Current Liabilities			
(*a*) Short-term Borrowings			
(*b*) Trade payables		6,18,000	
(*c*) Other Current Liabilities	5	41,100	
(*d*) Short-term Provisions		—	
TOTAL		18,41,100	
II. ASSETS			
(1) Non-Current Assets			
(*a*) Fixed Assets			
(*i*) Tangible Assets	6	8,05,400	
(*ii*) Intangible Assets			
(*b*) Non-current investments		2,50,000	
(*c*) Long-term Loans and Advances			
(*d*) Other Non-Current Assets			
(2) Current Assets			
(*a*) Current Investments			
(*b*) Inventories	7	4,70,000	
(*c*) Trade receivables	8	1,13,500	

(*d*) Cash and Bank Balance	9	1,94,000	
(*e*) Short-term Loans and Advances			
(*f*) Other Current Assets	10	8,200	
TOTAL		18,41,100	

Contingent Liability for Bills discounted but not matured ₹40,000.

Notes to Accounts :

			₹	₹
(1) **Share Capital :**				
Authorised Capital :				
.... Shares of ₹10 each				....
Issued Capital :				
.... Shares of ₹10 each				....
Subscribed Capital :				
Subscribed and Fully Paid Capital :				
53,000 Shares of ₹10 each			5,30,000	
Subscribed but not fully paid Capital				
10,000 Shares of ₹10 each		1,00,000		
Less : Calls-in-arrear		25,000	75,000	6,05,000
(2) **Reserves and Surplus :**				
General Reserve		1,54,000		
Less : Preliminary Expenses	30,000			
Brokerage on Shares	12,000	42,000	1,12,000	
Surplus			2,00,000	3,12,000
(3) **Long-term Borrowings :**				
15% Debentures			1,00,000	
Bank Loan			1,50,000	2,50,000
(4) **Long term Provisions :**				
Employees Benefit Fund				15,000
(It is assumed that Employees Benefit Fund is for more than 12 months)				
(5) **Other Current Liabilities :**				
Wages Due			29,000	
Godown Rent Due			3,600	
Salaries Due			3,500	
Unclaimed Dividends			5,000	41,100
(6) **Tangible Assets :**				
Land			80,000	
Building			2,12,500	
Machinery			5,08,000	
Livestock			4,900	8,05,400
(7) **Inventories :**				
Stores			90,000	

Stock in Trade	2,50,000	
Loose Tools	1,30,000	4,70,000
(8) Trade Receivables	1,20,000	
Less : Provision for Bad Debts	6,500	1,13,500
(9) **Cash and Bank Balance :**		
Cash at Bank	62,000	
Cash in Mill	7,000	
Cash in Office	1,25,000	1,94,000
(10) **Other Current Assets :**		
Unexpired Insurance		8,200

ILLUSTRATION [illegible]

The trainee accountant of John Smith and Company Ltd., who has gained a little knowledge of accounts, has drafted the following balance sheet :

BALANCE SHEET

for the year ended 31st March, 2022

Assets	*Amount*	*Liabilities*	*Amount*
	₹		₹
Land and Building	1,09,500	Capital — 18,000 Equity Shares	
Fixed Deposit accepted	15,000	of ₹10 each fully Called up	1,80,000
Furniture	30,000	Preliminary Expenses	22,000
Goodwill	10,000	10% Debentures	35,000
Inventories	24,000	Provision for Taxation	36,000
Sundry Creditors	9,000	Statement of Profit and Loss	
Machinery	25,000	Balance (Cr.)	48,000
Cash	38,000	Investment in Zee Ltd.	15,000
Bills Payable	7,000	Bills Receivable	7,000
Bank	72,000	Debtors	9,000
General Reserve	12,000	Unclaimed Dividends	
Calls in Arrear (on 1,000 Shares)	2,000	Authorised Capital — 20,000	
Securities Premium	10,000	Equity Shares of ₹10 each	11,000
		Share Forfeiture	500
	3,63,500		3,63,500

Additional Information : Proposed Dividend for the year 31st March 2022 was ₹14,000.

You are required to redraft the above Balance Sheet as per Schedule III Part I of Companies Act 2013.

SOLUTION :

John Smith and Company Ltd.

BALANCE SHEET *as at 31st March, 2022*

Particulars	*Note No.*	*31.3.2022* ₹	*31.3.2021* ₹
I. EQUITY AND LIABILITIES :			
(1) Shareholders' funds			
(*a*) Share capital	1	1,78,500	
(*b*) Reserves and surplus	2	48,000	
(2) Share application money pending allotment			
(3) Non-Current Liabilities			
(*a*) Long-term Borrowings	3	50,000	
(*b*) Other Long-term Liabilities			
(*c*) Long-term Provisions			
(4) Current Liabilities			
(*a*) Short-term Borrowings			
(*b*) Trade payables	4	16,000	
(*c*) Other Current Liabilities	5	11,000	
(*d*) Short-term Provisions	6	36,000	
TOTAL		3,39,500	
II. ASSETS			
(1) Non-Current Assets			
(*a*) Fixed Assets			
(*i*) Tangible Assets	7	1,64,500	
(*ii*) Intangible Assets	8	10,000	
(*b*) Non-current investments	9	15,000	
(*c*) Long-term Loans and Advances			
(*d*) Other Non-Current Assets			
(2) Current Assets			
(*a*) Current Investments			
(*b*) Inventories		24,000	
(*c*) Trade receivables	10	16,000	
(*d*) Cash and Bank Balance	11	1,10,000	
(*e*) Short-term Loans and Advances			
(*f*) Other Current Assets			
TOTAL		3,39,500	

Notes to Accounts :

	₹	₹
(1) **Share Capital :**		
Authorised		
20,000 Equity Shares of ₹10 each		2,00,000
Issued		
.... Equity Shares of ₹10 each		....

Subscribed Capital :			
Subscribed and Fully Paid Share Capital :			
17,000 Equity Shares of ₹10 each		1,70,000	
Subscribed but not Fully Paid Capital :			
1,000 Equity Shares of ₹10 each fully Called up	10,000		
Less : Calls in arrears	2,000	8,000	
		1,78,000	
Add : Share Forfeiture A/c		500	1,78,500
(2) **Reserves and Surplus :**			
Securities Premium	10,000		
General Reserve	12,000		
	22,000		
Less : Preliminary Exp.	22,000	—	
Surplus		48,000	48,000
(3) **Long-term Borrowings :**			
10% Debentures		35,000	
Fixed Deposits Accepted (Assumed for more than 12 months)		15,000	50,000
(4) **Trade Payables :**			
Bills Payable		7,000	
Sundry Creditors		9,000	16,000
(5) **Other Current Liabilities :**			
Unclaimed Dividends			11,000
(6) **Short-term Provisions :**			
Provision for Taxation			36,000
(7) **Tangible Assets :**			
Land and Building		1,09,500	
Machinery		25,000	
Furniture		30,000	1,64,500
(8) **Intangible Assets :**			
Goodwill			10,000
(9) **Non Current Investments :**			
Investments in Zee Ltd.			15,000
(10) **Trade Receivables :**			
Bills Receivables		7,000	
Debtors		9,000	16,000
(11) **Cash and Bank Balance :**			
Bank		72,000	
Cash		38,000	1,10,000

Note : Contingent Liability for Proposed Dividend ₹14,000.

It will be necessary to ascertain net balance of 'Surplus' in notes to accounts. This is, because the Statement of Profit & Loss is prepared to calculate the divisible profit (*i.e.*, net profit) whereas appropriations will be made in notes to accounts to calculate the net balance of 'Surplus' to be taken to 'Reserve and Surplus' in the Balance Sheet.

Divisible Profits

All profits are not divisible profits. Only those profits which are legally available to shareholders for dividend are known as divisible profits. In normal course, divisible profits are the profits left after meeting all expenses, losses, depreciation on fixed assets, fall in the price of current assets, taxation and after writing off past losses. Divisible profits should not include capital profits *i.e.*, the profits of extraordinary nature (non-recurring profits) or profits arising from revaluation or sale of fixed assets or redemption of fixed liabilities. Dividends cannot be declared except out of divisible profits.

Surplus Account

After ascertaining the divisible profits, the question of its disposal arises. Usually, the articles of the Company empower the directors to decide the amount of profit to be transferred to reserves and also the quantum of dividends. The directors may decide to retain a certain amount of profits to strengthen the financial position of the Company. Such profits may be retained in the form of transfer to various reserves or even by keeping as a balance. A part of the profits may also be distributed as dividends. As such, 'Net Surplus' will have to be calculated (in notes to accounts) by making various appropriations as follows :

RESERVE AND SURPLUS

		₹	₹
	Last year's Surplus		....
Add :	Current year's Surplus (*i.e.*, Profit for the current year)		....
Add :	Transfer from Reserve (if any)	....	
Add :	Adjustments relating to past years, such as saving in provision for Taxation in previous years	....	....
			....
Less :	Transfer to Reserves :		
	1. Transfer to General Reserve	....	
	2. Transfer to Development Rebate Reserve	....	
	3. Transfer to Dividend Equalisation reserve	....	
	4. Transfer to Debenture Redemption Fund etc.	....	
Less :	Adjustments relating to past years, such as, arrears of Depreciation	....	
Less :	Interim Dividend on Equity Shares	....	
	Closing Balance of Surplus Carried to Balance Sheet under the head 'Reserve and Surplus'		....

Items shown as deduction from Surplus A/c :—

1. **Transfer to various reserves**, such as, General Reserve, Dividend Equalisation Fund, Debenture Redemption Fund etc.
2. **Interim Dividend** : Dividend paid during the year, before ascertainment of the profits for the year is called '**Interim Dividend**'. Directors are empowered

to pay the interim dividend, in anticipation of the profits and without the sanction from the shareholders. However, if an interim dividend is paid and it is found subsequently that the Company's profits are inadequate to cover the interim dividend, it amounts to payment of dividend out of capital which is forbidden by law and hence the directors will be liable to make good the amount.

Balance of 'Surplus' is shown on the equity and liabilities side of the balance sheet under the heading 'Reserves and Surplus'.

PROPOSED DIVIDEND

Dividend proposed by directors is termed as proposed dividend.

As per Revised AS-4, Contingencies and Events Occurring after the Balance Sheet date, proposed dividend is not provided in the books but it is shown in the Notes to Accounts as Contingent Liability because it will be declared (approved) by shareholders (and not by directors) at the Annual General Meeting to be held after the end of financial year *i.e.*, in the next financial year.

Final Dividend : Dividend proposed by the directors is declared by shareholders (and not by directors) at the annual general meeting. After the declaration the proposed dividend is termed as final dividend. Shareholders cannot increase the rate of dividend proposed by the directors.

ILLUSTRATION 21.

For the year ended 31st March, 2020, the profit of '*A*' Ltd. before charging depreciation on fixed assets amounted to ₹9,20,000. Depreciation amounted to ₹2,00,000. The paid up capital of the company consisted of 30,000 6% preference shares of ₹100 each and 4,00,000 equity shares of ₹10 each. Interim dividend on equity shares was paid during the year at 7.5%. There was a credit balance of ₹4,10,000 brought forward from the previous year. **The following appropriations were porposed by the directors of the Company** :

1. To provide for taxation ₹2,00,000.
2. To transfer 2.5% of Current year's profit to General Reserve.
3. To pay the year's dividend on preference shares.
4. To pay a final (additional) dividend of 5% on equity share capital.
5. To carry forward the balance.

Write up the 'Reserve and Surplus' to be shown in notes to accounts.

SOLUTION :

STATEMENT OF PROFIT & LOSS
for the year ended 31st March, 2020

	₹	₹
Net Profit for the year brought forward		9,20,000
Less : Depreciation	2,00,000	
Provision for Taxation	2,00,000	4,00,000
Net Profit after tax		5,20,000

Notes to Accounts :

Reserve and Surplus :

		₹	₹
Last year's Surplus			4,10,000
Current year's Surplus			5,20,000
			9,30,000
Less :	Transfer to General Reserve (2.5% of ₹5,20,000)	13,000	
	Interim Dividend @ 7.5% on Equity Capital of ₹40,00,000	3,00,000	3,13,000
Balance of Surplus carried to Balance Sheet under the head 'Reserve and Surplus'			6,17,000

Note : Contingent Liability :

		₹
For Porposed Dividend on Pref. Share Capital 6% on ₹30,00,000	=	1,80,000
For Proposed Final Dividend on Equity Share Capital 5% on ₹40,00,000	=	2,00,000
Total		3,80,000

Some necessary Adjustments for preparation of Financial Statements of Companies :—

1. **Proposed Dividend :**— It will be shown as a Contingent Liability in Notes to Accounts.

2. **Interim Dividend :**—If directors pay dividend even before the year is closed and the payment is out of current year's profit, it is called interim dividend. It is usually given on the debit side of the Trial Balance and because it is an appropriation of profits, it is recorded as a deduction from 'Surplus' in Notes to Accounts.

3. **Unclaimed Dividend :**— This always appears on the credit side of Trial Balance and represents dividend not collected by the shareholders. It is recorded on the equity & liability side of the balance sheet under the heading 'Current Liabilities' under sub-head 'Other Current Liabilities'.

ILLUSTRATION 22.

Hindustan Agro Ltd. was registered with an authorised capital of 8,00,000 shares of ₹10 each. 6,00,000 shares were issued to the public out of which 5,00,000 shares were taken up. The following balances appeared in the books of the Company as on 31st March, 2022 :

	₹
Share Capital 5,00,000 Shares of ₹10 each, ₹5 called up	25,00,000
Calls in Arrear	10,000
Calls in Advance	15,000
Profit & Loss balance (on 1.4.2021)	3,50,000
12% Debentures	5,00,000
Unsecured Loan	1,50,000
Cash in Hand	12,800
Balance with Banks	20,700
Sundry Debtors	
More than six months old	25,000

Other Debtors	3,50,000
Sundry Creditors	1,82,200
Provision for Taxation	75,000
Net Profit for the Year (after tax)	7,20,000
Freehold Premises	16,00,000
Plant & Machinery	18,50,000
Patents	10,000
Goodwill	2,00,000
Preliminary Expenses	44,800
Prepaid Expenses	5,000
Outstanding Expenses	66,000
Investment in Shares	53,000
Closing Stock	3,64,100
Bills Receivable	20,000
Bills Payable	7,200

Prepare the Company's Balance Sheet for the year ended 31st March, 2022 in prescribed Form after taking into account the following matters :

(*a*) Transfer to General Reserve ₹3,00,000.

(*b*) Directors proposed a dividend of 10% on share capital.

SOLUTION :

Hindustan Agro Ltd.
BALANCE SHEET
as at 31st March, 2022

Particulars	*Note No.*	*31.3.2022* ₹	*31.3.2021* ₹
I. EQUITY AND LIABILITIES :			
(1) Shareholders' funds			
(*a*) Share capital	1	24,90,000	
(*b*) Reserves and surplus	2	10,25,200	
(2) Share application money pending allotment			
(3) Non-Current Liabilities			
(*a*) Long-term Borrowings	3	6,50,000	
(*b*) Other Long-term Liabilities			
(*c*) Long-term Provisions			
(4) Current Liabilities			
(*a*) Short-term Borrowings			
(*b*) Trade payables	4	1,89,400	
(*c*) Other Current Liabilities	5	81,000	
(*d*) Short-term provisions	6	75,000	
TOTAL		45,10,600	
II. ASSETS :			
(1) Non-Current Assets			
(*a*) Fixed Assets			
(*i*) Tangible Assets	7	34,50,000	
(*ii*) Intangible Assets	8	2,10,000	

(*b*) Non-current Investments		53,000	
(*c*) Long-term Loans and Advances			
(*d*) Other Non-Current Asset			
(2) **Current Assets**			
(*a*) Current Investments			
(*b*) Inventories		3,64,100	
(*c*) Trade receivables	9	3,95,000	
(*d*) Cash and Bank Balance	10	33,500	
(*e*) Short-term Loans and Advances			
(*f*) Other Current Assets	11	5,000	
TOTAL		45,10,600	

Notes to Accounts

		₹	₹
(1) **Share Capital :**			
Authorised Capital :			
8,00,000 shares of ₹10 each		80,00,000	
Issued Capital : 6,00,000 shares of ₹10 each		60,00,000	
Subscribed but not Fully Paid Capital :			
5,00,000 shares of ₹10 each ₹5 called-up	25,00,000		
Less : Calls in Arrears	10,000		24,90,000
(2) **Reserve and Surplus :**			
General Reserve	3,00,000		
Less : Preliminary Expenses	44,800		2,55,200
Profit & Loss Balance on 1-4-2021		3,50,000	
Current Year's Profit		7,20,000	
		10,70,000	
Less : Transfer to General Reserve		3,00,000	7,70,000
			10,25,200
(3) **Long-term Borrowings :**			
12% Debentures		5,00,000	
Unsecured Loan		1,50,000	6,50,000
(4) **Trade Payables :**			
Sundry Creditors		1,82,200	
Bills Payable		7,200	1,89,400
(5) **Other Current Liabilities :**			
Calls in Advance		15,000	
Outstanding Expenses		66,000	81,000
(6) **Short-term Provisions :**			
Provision for Taxation			75,000
(7) **Tangible Assets :**			
Freehold Premises		16,00,000	

Plant & Machinery		18,50,000	34,50,000
(8) **Intangible Assets :**			
Patents		10,000	
Goodwill		2,00,000	2,10,000
(9) **Trade Receivables :**			
Sundry Debtors :			
More than Six Months old	25,000		
Other Debtors	3,50,000	3,75,000	
Bills Receivable		20,000	3,95,000
(10) **Cash and Bank Balance**			
Balance with Banks		20,700	
Cash in Hand		12,800	33,500
(11) **Other Current Assets :**			
Prepaid Expenses			5,000

(12) Contingent Liability for Proposed Dividend on Equity Share Capital is ₹2,49,000. (10% on 24,90,000 *i.e.*, Share Capital ₹25,00,000 *less* Calls in Arrear ₹10,000)

ILLUSTRATION 22

The following balances are left on the books of Five Star Fashions Ltd. after its Profit & Loss Statement has been prepared for the year ended 31st March, 2022.

	₹		₹
Public Deposits	1,50,000	Sundry Debtors	5,20,000
Interest accrued but not due	2,500	Security Deposit	80,000
Bank Overdraft	2,36,600	Interest Accrued on Investments	6,000
Trade Payables	1,75,000	Plant and Machinery	15,40,000
General Reserve	2,00,000	Vehicles	3,10,000
1,60,000 Equity Shares of ₹10 each	16,00,000	10% Government Bonds	60,000
		Loan to Staff	25,000
5,000, 10% Preference Shares of ₹100 each	5,00,000	Inventories	4,10,700
		Prepaid Insurance	1,000
Securities Premium	2,00,000	Share Issue Expenses	5,000
10% Secured Loan	1,80,000	B/R	22,000
Interest Accrued and due on Secured Loan	4,800	Cash and Bank Balance	15,400
		Land and Building	6,44,000
Net Profit for the year ended 31st March, 2022	3,20,000		
Expenses Owing	12,200		
Employees' Benefit Fund	20,000		
Sinking Fund	38,000		
	36,39,100		36,39,100

Note : Bills Receivable discounted but not matured ₹15,000.

It was resolved that :

(*a*) The General Reserve be increased to ₹2,50,000.

(*b*) A dividend of 8% on Equity Share Capital and 10% on Preference Share Capital be proposed.

Prepare the Company's Balance Sheet as on 31st March, 2022.

SOLUTION

FIVE STAR FASHIONS LTD.

BALANCE SHEET

as at 31st March, 2022

Particulars	*Note No.*	*31.3.2022* ₹	*31.3.2021* ₹
I. EQUITY AND LIABILITIES :			
(1) **Shareholders' funds**			
(*a*) Share capital	2	21,00,000	
(*b*) Reserves and surplus	3	7,53,000	
(2) **Share application money pending allotment**			
(3) **Non-Current Liabilities**			
(*a*) Long-term Borrowings	4	3,30,000	
(*b*) Other Long-term Liabilities			
(*c*) Long-term Provisions	5	20,000	
(4) **Current Liabilities**			
(*a*) Short-term Borrowings	6	2,36,600	
(*b*) Trade payables		1,75,000	
(*c*) Other Current Liabilities	7	19,500	
TOTAL		36,34,100	
II. ASSETS :			
(1) **Non-Current Assets**			
(*a*) Fixed Assets			
(*i*) Tangible Assets	8	24,94,000	
(*ii*) Intangible Assets			
(*b*) Non-current Investments	9	60,000	
(*c*) Long-term Loans and Advances	10	1,05,000	
(*d*) Other Non-Current Asset			
(2) **Current Assets**			
(*a*) Current Investments			
(*b*) Inventories		4,10,700	
(*c*) Trade receivables	11	5,42,000	
(*d*) Cash and Bank Balance		15,400	
(*e*) Short-term Loans and Advances			
(*f*) Other Current Assets	12	7,000	
TOTAL		36,34,100	

Notes to Accounts :

	₹	₹
(1) Contingent Liabilities for Bills Discounted but not matured amount to ₹15,000.		
(2) **Share Capital :**		
Authorised :		
.... shares of ₹......... each	....	
Issued :		
.... shares of ₹......... each	....	
Subscribed and fully paid up :		
5,000, 10% Preference Shares of ₹100 each	5,00,000	
1,60,000 Equity Shares of ₹10 each	16,00,000	21,00,000
(3) **Reserves and Surplus :**		
Securities Premium	2,00,000	
Less : Share Issue Exp.	5,000	1,95,000
Sinking Fund		38,000
General Reserve	2,00,000	
Add : Addition	50,000	2,50,000
Current Year's Profit	3,20,000	
Less : Transfer to General Reserve	50,000	2,70,000
		7,53,000
(4) **Long-term Borrowings :**		
10% Secured Loan	1,80,000	
Public Deposits (Assumed for more than one year)	1,50,000	3,30,000
(5) **Long term Provisions :**		
Employess Benefit Fund (assumed for more than one year)		20,000
(6) **Short-term Borrowings :**		
Bank Overdraft		2,36,600
(7) **Other Current Liabilities :**		
Interest Accrued but not due	2,500	
Interest Accrued and due on Secured Loan	4,800	
Expenses Owing	12,200	19,500
(8) **Tangible Assets :**		
Land and Building	6,44,000	
Plant and Machinery	15,40,000	
Vehicles	3,10,000	24,94,000
(9) **Non Current Investments :**		
10% Government Bonds		60,000
(10) **Long-term Loans and Advances :**		
Security Deposit	80,000	

Loan to Staff		25,000	1,05,000
(11) **Trade Receivables :**			
Sundry Debtors		5,20,000	
B/R		22,000	5,42,000
(12) **Other Current Assets :**			
Interest Accrued on Investments		6,000	
Prepaid Insurance		1,000	7,000
(13) **Contingent Liability :**			
Proposed Dividend			
On Pref. Share Capital ₹5,00,000 × 10%	50,000		
On Equity Share Capital ₹16,00,000 × 8%	1,28,000		
	1,78,000		

ILLUSTRATION 24.

Pokemon Ltd. had an authorised Capital of 25,000 Shares of ₹25 each and 15,000, 5% Preference Shares of ₹10 each. All the Shares were issued and fully paid up. The Company had a balance of profit ₹4,25,000 brought forward from the last year and the net profit for the year ended 31st March, 2022 was ₹2,40,000. The Directors have proposed to make the following appropriations from the balance available :

(*i*) To pay the year's dividend on the Preference Shares;

(*ii*) To pay a dividend of 12% on the equity shares.

(*iii*) To transfer ₹45,000 to General Reserve;

(*iv*) To write off the balance of ₹25,000 on Goodwill Account;

(*v*) To transfer ₹15,000 to Staff Welfare Fund.

You are required to show how the items will appear in the Balance Sheet of the Company and prepare 'Notes to Accounts'.

SOLUTION :

Pokemon Ltd.

BALANCE SHEET *as at 31st March, 2022*

(Equity & Liabilities side only)

Particulars	*Note No.*	*31.3.2022* ₹	*31.3.2021* ₹
I. EQUITY AND LIABILITIES :			
(1) Shareholders' funds			
(*a*) Share capital	1	7,75,000	
(*b*) Reserves and surplus	2	6,25,000	
(2) Share application money pending allotment			
(3) Non-Current Liabilities			
(*a*) Long-term Borrowings			
(*b*) Other Long-term Liabilities			
(*c*) Long-term Provisions	3	15,000	

(4) Current Liabilities			
(*a*) Short-term Borrowings			
(*b*) Trade payables			
(*c*) Other Current Liabilities			
TOTAL		14,15,000	

Notes to Accounts :

		₹	₹
(1) **Share Capital :**			
Authorised, issued, subscribed and fully paid :			
25,000 equity shares @₹25 each fully paid		6,25,000	
15,000, 5% Preference Shares @₹10 each fully paid		1,50,000	7,75,000
(2) **Reserve and Surplus :**			
General Reserve			45,000
Last Year's Surplus		4,25,000	
Current Year's Surplus		2,40,000	
		6,65,000	
Less : Goodwill Written off	25,000		
Transfer to Staff Welfare Fund	15,000		
Transfer to General Reserve	45,000	85,000	5,80,000
			6,25,000
(3) **Long term Provisions :**			
Staff Welfare Fund (Assumed for more than one year)			15,000
(4) **Contingent Liabilities :**			
Proposed Dividend on Preference Capital @ 5% on ₹1,50,000		7,500	
Proposed Dividend on Equity Capital @ 12% on ₹6,25,000		75,000	82,500

ILLUSTRATION 25.

Pinnacle Instruments Ltd. registered itself with a capital of ₹20,00,000 divided into Equity Shares of ₹100 each.

On 1st June, 2014, the company issued 5,000 Equity Shares as fully paid to Mila Herbals, as purchase consideration for the purchase of plant and machinery.

The remaining shares were issued to the public at par.

Till the date of the Balance Sheet, the Directors had called from the public, 60% of the nominal value of the shares.

The amount called was received by the company.

You are required to prepare as at 31st March, 2015 :

(*i*) The Balance Sheet of Pinnacle Instruments Ltd. as per Schedule III of the Companies Act, 2013.

(*ii*) Notes to Accounts.

(ISC 2016)

SOLUTION

BALANCE SHEET OF PINNACLE INSTRUMENTS LTD.

as at 31st March, 2015

Particulars	*Note No.*	*31.3.2015* ₹	*31.3.2014* ₹
I. EQUITY AND LIABILITIES :			
(1) **Shareholder's Funds**			
(*a*) Share Capital	1	14,00,000	
		14,00,000	
II. ASSETS			
(1) **Non-Current Assets**			
(*a*) Fixed Assets			
(*i*) Tangible Assets	2	5,00,000	
(2) **Current Assets**			
(*a*) Cash and Bank Balances	3	9,00,000	
TOTAL		14,00,000	

Notes to Accounts :

Particulars	₹
(1) **Share Capital**	
Authorised Capital	
20,000 Equity Shares of ₹100 each	20,00,000
Issued Capital	
20,000 Equity Shares of ₹100 each	20,00,000
Subscribed Capital	
Subscribed and Fully Paid Capital	
5,000 Shares @ ₹100 each	5,00,000
(Issued as fully paid up for purchase of Plant & Machinery	
Subscribed but not Fully Paid Capital	
15,000 Shares @ ₹100 each, ₹60 Called up	9,00,000
	14,00,000
(2) **Fixed Assets (Tangible)**	
Plant and Machinery	5,00,000
(3) **Cash and Bank Balances**	
Cash at Bank	9,00,000

ILLUSTRATION 26.

Palms Ltd. was formed on 1st November, 2015, with a capital ₹12,00,000 divided into Equity Shares of ₹10 each at a premium of ₹2 per share. It offered 1,00,000 shares to the public.

The issue price was payable as follows :

₹4 with application
₹6 with allotment (including premium)
The balance as and when required.

The balance was not called till the date of the Balance Sheet.

All the shares offered by the company were subscribed for. One shareholder holding 1,000 shares paid the balance with allotment.

Another shareholder holding 800 shares did not pay the allotment money when due.

You are required to show the items under Equity and Liabilities in the Balance Sheet of the Company (prepared as per Schedule III of the Companies Act 2013) at the end of the financial year with Notes to Accounts. *(ISC Sample Paper, 2017)*

BALANCE SHEET OF PALMS LTD.
as at 31st March, 2016

Particulars	*Note No.*	*31.3.2016* ₹	*31.3.2015* ₹
I. EQUITY AND LIABILITIES :			
Shareholder's Funds			
(*a*) Share Capital	1	7,96,800	
(*b*) Reserve and Surplus	2	1,98,400	
Current Liabilities :			
Other Current Liabilities	3	2,000	
TOTAL		9,97,200	

Notes to Accounts :

		₹
(1) **Share Capital**		
Authorised :		
1,20,000 Equity Shares of ₹10 each		12,00,000
Issued :		
1,00,000 Equity Shares of ₹10 each		10,00,000
Subscribed but not Fully Paid Capital :		
1,00,000 Equity Shares of ₹10 each ₹8 Called up	8,00,000	
Less : Calls in Arrears	3,200	7,96,800
(2) **Reserve and Surplus :**		
Securities Premium Reserve	2,00,000	
Less : Calls in Arrears	1,600	1,98,400
(3) **Other Current Liabilities :**		
Calls in Advance (1,000 × ₹2)		2,000

ILLUSTRATION 27.

Following balances have been extracted from the books of Universe Ltd. as at 31st March, 2016 :

Particulars	*Amount*
	₹
Equity Share Capital (Fully paid shares of ₹100 each)	4,00,000
Unclaimed Dividend	10,000
Bank Balance	40,000
Security Premium Reserve	75,000
Statement of Profit and Loss (Dr.)	50,000
Tangible Fixed Assets (at cost)	3,50,000
Accumulated Depreciation till date	25,000
Trade Marks	70,000

You are required to prepare as at 31st March, 2016 :

(*i*) The Balance Sheet of Universe Ltd. as per Schedule III of the Companies Act, 2013.

(*ii*) Notes to Accounts. *(I.S.C. 2017)*

SOLUTION : BALANCE SHEET OF UNIVERSE LTD.

as at 31st March, 2016

Particulars	*Note No.*	*31.3.2016* ₹	*31.3.2015* ₹
I. EQUITY AND LIABILITIES :			
(1) **Shareholders' Funds**			
(*a*) Share Capital	1	4,00,000	
(*b*) Reserves and Surplus	2	25,000	
(2) **Current Liabilities**			
Other Current Liabilities	3	10,000	
TOTAL		4,35,000	
II. ASSETS			
(1) **Non-Current Assets**			
Fixed Assets			
(*i*) Tangible Assets	4	3,25,000	
(*ii*) Intangible Assets	5	70,000	
(2) **Current Assets**			
Cash and Bank Balance		40,000	
TOTAL		4,35,000	

Notes to Accounts :

	₹
1. **Share Capital**	
Authorised Capital	
.... Equity Shares @ ₹100	

Issued Capital	
.... Equity Shares @ ₹100	
Subscribed Capital	
Subscribed and fully paid up	
4,000 Equity Shares @ ₹100	4,00,000
2. **Reserves and Surplus**	
Security Premium Reserve	75,000
Less : Statement of P & L (Dr.)	(50,000)
	25,000
3. **Other Current Liabilities**	
Unclaimed Dividend	10,000
4. **Tangible Assets**	
At Cost	3,50,000
Less : Accumulated Depreciation	(25,000)
	3,25,000
5. **Intangible Assets**	
Trade Marks	70,000

ILLUSTRATION [illegible]

Ajmera Ltd. raised the following loans in the year 2016-17 :

12% Bank Loan from SBI on 1st April, 2016 :	₹15,00,000
10,000; 10% Debentures of ₹100 each, redeemable at par in 4 equal yearly instalments, on 1st October, 2016 :	₹10,00,000

The terms of the loans were :

(*i*) The redemption of Debentures to begin from 30th September, 2017.

(*ii*) Interest on the Bank Loan to be paid annually but interest on Debentures to be paid half-yearly.

The company had not paid the interest, both on the Bank Loan and on the Debentures, till the Balance Sheet date.

You are required to show the above items under Equity and Liabilities of the Balance Sheet of the company as at 31st March, 2017.

(I.S.C. Specimen Question Paper 2018)

SOLUTION : EXTRACT OF BALANCE SHEET OF AJMERA LTD.
as at 31st March, 2017

Particulars	*Note No.*	*31st March 2017 (₹)*	*31st March, 2016 (₹)*
I. EQUITY AND LIABILITIES :			
(1) Shareholder's Funds			
(2) Non-Current Liabilities			
Long-term Borrowings	1	22,50,000	

(3) **Current Liabilities**		
Other Current Liabilities	2	4,80,000

Notes to Accounts

Particulars		₹
1. **Long-term Borrowings :**		
7,500; 10% Debentures of ₹100 each	7,50,000	
Long-term Loan :		
12% Bank Loan from SBI	15,00,000	22,50,000
2. **Other Current Liabilities :**		
(*a*) Current Maturities of Long-term Debts (2,500, 10% Debentures of ₹100 each redeemable on 30th Sept. 2017)	2,50,000	
(*b*) Interest Accrued and Due on Borrowings		
10% on 10,000 Debentures of ₹100 each for six months	50,000	
12% on Bank Loan of ₹15,00,000 for one year	1,80,000	4,80,000

ILLUSTRATION 29

The following balances have been extracted from the books of Vanity Ltd. as at 31st March, 2017 :

TRIAL BALANCE
as at 31st March, 2017

Particulars	*Debit* ₹	*Credit* ₹
Equity Share Capital (5,000 shares of ₹100 each fully paid)		5,00,000
Fixed Assets	7,30,000	
Reserves and Surplus		2,00,000
Inventories	50,000	
Cash and Bank Balances	1,70,000	
Creditors		40,000
Bills Payable		20,000
Underwriting Commission on issue of shares	10,000	
5% Debentures (1/5 of the Debentures to be redeemed on 31st March, 2018)		2,00,000
Provision for Taxation		12,000
Interest accrued and due on 5% Debentures		8,000
Trade Receivables	20,000	
TOTAL	9,80,000	9,80,000

You are required to prepare as at 31st March, 2017 :

(*i*) The Balance Sheet of Vanity Ltd. as per Schedule III of the Companies Act, 2013.

(*ii*) Notes to Accounts. *(I.S.C. 2018)*

SOLUTION :

BALANCE SHEET OF VANITY LTD.

as at 31st March, 2017

Particulars	*Note No.*	*31.3.2017* (₹)	*31.3.2016* (₹)
I. EQUITY AND LIABILITIES :			
(1) **Shareholder's Funds**			
(*a*) Share Capital	1	5,00,000	
(*b*) Reserves and Surplus	2	1,90,000	
(2) **Non-Current Liabilities**			
Long-term Borrowings	3	1,60,000	
(3) **Current Liabilities**			
(*a*) Trade Payables	4	60,000	
(*b*) Other Current Liabilities	5	48,000	
(*c*) Short Term Provisions	6	12,000	
TOTAL		9,70,000	
II. ASSETS :			
(1) **Non-Current Assets**			
Fixed Assets		7,30,000	
(2) **Current Assets**			
(*a*) Inventories		50,000	
(*b*) Trade Receivables		20,000	
(c) Cash and Bank Balances		1,70,000	
TOTAL		9,70,000	

Notes to Accounts :

Particulars		₹
1. **Share Capital**		
Authorized Capital		
.... Equity Shares @₹100		....
Issued Capital		
..............Equity Shares @₹100		....
Subscribed and fully paid up		
5,000 Equity Shares @₹100		5,00,000
2. Reserves and Surplus	2,00,000	
Less : Underwriting commission	(10,000)	1,90,000
3. **Long term borrowings :**		
5% Debentures (4/5th of ₹2,00,000)		1,60,000
4. **Trade Payables :**		
Creditors	40,000	
Bills Payable	20,000	60,000
5. **Other Current Liabilities :**		
Current Maturity of Long Term Debts — 5% Debentures (1/5th of 2,00,000)	40,000	
Interest Accrued and Due on 5% Debentures	8,000	48,000

6. **Short Term Provisions :**	
Provision for Taxation	12,000

ILLUSTRATION 32.

The trainee accountant of Rudra Ltd. drafted the following Balance Sheet. He did not prepare it according to the format prescribed as per Schedule III of the Companies Act, 2013. He also classified a few items incorrectly.

BALANCE SHEET OF RUDRA LTD.
for the year ending 31st March, 2018

Assets	*Amount*	*Liabilities*	*Amount*
	₹		₹
General Reserve	1,20,000	Capital (1,30,000 Equity Shares @ ₹10 each)	13,00,000
Plant & Machinery	6,00,000	Share Forfeiture	10,000
Land & Building	8,00,000	Goodwill	1,00,000
Profit & Loss (Debit Balance)	1,50,000	Trade Receivables	20,000
Cash & Bank Balances	2,50,000	Trade Payables	50,000
Unclaimed Dividend	30,000	Inventories	30,000
Calls-in-arrears (₹4 per share)	40,000	Fixed Deposit accepted	4,50,000
		Calls-in-advance	30,000
	19,90,000		19,90,000

Foot note : The company had an authorized capital of 2,00,000 Equity shares of ₹10 each.

You are required to prepare, as at 31st March, 2018 :

(*i*) The Balance Sheet of Rudra Ltd. as per Schedule III of the Companies Act, 2013.

(*ii*) Notes to Accounts. (*I.S.C. 2019*)

SOLUTION :

BALANCE SHEET OF RUDRA LTD.
As at 31st March, 2018

Particulars	*Note No.*	*31.3.2018* (₹)	*31.3.2017* (₹)
I. EQUITY AND LIABILITIES :			
(1) Shareholder's Funds			
(*a*) Share Capital	1	12,70,000	
(*b*) Reserves and Surplus	2	(30,000)	
(2) Non-Current Liabilities			
Long-term Borrowings			
(Fixed Deposits Accepted)		4,50,000	
(3) Current Liabilities			
(*a*) Trade Payables		50,000	

(*b*) Other Current Liabilities	3	60,000
TOTAL		18,00,000
II. ASSETS :		
(1) **Non-Current Assets**		
Fixed Assets	4	
(*i*) Tangible		14,00,000
(*ii*) Intangible (Goodwill)		1,00,000
(2) **Current Assets**		
(*a*) Inventories		30,000
(*b*) Trade Receivables		20,000
(c) Cash and Bank Balances		2,50,000
TOTAL		18,00,000

Notes to Accounts

Particulars		₹
1. **Share Capital**		
Authorised Capital		
2,00,000 Equity Shares of ₹10 each		20,00,000
Issued Capital		
...... Equity Shares of ₹10 each		....
Subscribed Capital		
Subscribed and Fully Paid :		
1,20,000 Equity Shares of ₹10 each		12,00,000
Subscribed but not Fully Paid :		
10,000 Equtiy Shares of ₹10 each fully Called up	1,00,000	
Less : Calls-in-arrears	(40,000)	
Add : Share Forfeiture A/c	10,000	70,000
		12,70,000
2. **Reserves & Surplus :**		
General Reserve		1,20,000
Statement of Profit & Loss (Dr. Balance)		(1,50,000)
		(30,000)
3. **Other Current Liabilities :**		
Unclaimed Dividend		30,000
Calls-in-advance		30,000
		60,000
4. **Fixed Assets (Tangible) :**		
Land & Building		8,00,000
Plant & Machinery		6,00,000
		14,00,000

SHORT ANSWER QUESTIONS

(Questions Carrying 2 Marks)

1. Name the major headings under which the Equity & Liabilities and the Assets sides of a Company's Balance Sheet are organised and presented.

[Ans. (*a*) The major headings on the Equity & Liabilities side are :

I. Shareholder's Funds
II. Share Application money pending allotment.
III. Non-Current Liabilities
IV. Current Liabilities

(*b*) The major headings on the Assets side are :

I. Non-Current Assets.
II. Current Assets.]

2. Prepare a layout of information required to be given under the heading 'Share Capital' on the equity & liabilities side of a Company's Balance Sheet.

3. What items are required to be included under the heading "Current Assets"?

4. What items are required to be included under the heading "Current Liabilities"?

5. What is a Contingent liability? Give one example. *(I.S.C. 2002)*

6. List two items each under the headings 'Non-Current Liabilities' and 'Non-Current Assets' in a Balance Sheet prepared as per schedule III of the Companies Act.

7. What are miscellaneous expenses? *(I.S.C. 2007)*

Ans. These are the part of expenses which are not written off up to the date of the Balance Sheet. These include the following :

(*i*) Preliminary Expenses;

(*ii*) Expenses including commission or brokerage on underwriting of issue of shares or debentures;

(*iii*) Discount allowed on issue of debentures;

(*iv*) Interest paid out of capital, and

(*v*) Development expenditure not adjusted.

8. When drafting a company's balance sheet under Schedule III Part I, under which heading and sub-heading will calls in arrear and calls in advance appear?

Ans.

	Heading	*Sub-heading*
(*i*) Call in Arrears	Shareholder's Funds	This will be deducted from subscribed but not fully paid capital
(*ii*) Calls in Advance	Current Liabilities	Other Current Liabilities

9. Give two examples of intangible fixed assets. *(I.S.C. 2009)*

Ans. (*i*) Goodwill (*ii*) Patents.

10. Give four examples of tangible fixed assets as per Schedule III, Part I of the Companies Act, 2013.

Ans. (*i*) Machinery (*ii*) Land (*iii*) Buildings (*iv*) Leaseholds

11. What are fictitious assets? Give one example? *(ISC 2010)*

Ans. These are the Assets which cannot be realised in Cash or no further benefit can be derived from these assets. Such assets include preliminary expenses, discount on issue of shares and debentures and the expenditure not yet written off such as Advertisement Expenses etc.

12. What is divisible profit?

13. What are trade investments? *(ISC 2012)*

Ans. Schedule III requires that non-current investments shall be classified as "Trade Investments" and "Other Investments". The term trade investment is defined neither in Schedule III nor in Accounting Standards.

The term "trade investments" is, however, normally understood as an investment made by a company in shares or debentures of another company, to promote the trade or business of the first company.

14. What is meant by an operating cycle? *(ISC 2015)*

Ans. (*i*) An operating cycle is the time between the acquisition of assets for processing and their realization in cash or cash equivalents.

(*ii*) When the normal operating cycle cannot be identified, it is assumed to have a duration of 12 months.

15. Mention whether the following Trade Payables are current liabilities or non current liabilities :

	Operating Cycle	*Expected Period of Payment*
(*a*)	12 months	14 months
(*b*)	15 months	12 months

(I.S.C. 2018)

Ans. (*a*) Non Current Liability; (b) Current Liability.

16. Under which heads and sub-heads will the following items appear in the Balance Sheet of a company as per Schedule III of the Companies Act, 2013:

(*i*) Public Deposits

(*ii*) Calls-in-Advance *(C.B.S.E. 2018, C)*

(*iii*) Building under construction *(ISC 2016)*

Ans.

Item	*Head*	*Sub-head*
(*i*) Public Deposits	Non Current Liability	Long Term Borrowing
(*ii*) Calls-in-Advance	Current Liability	Other Current Liability
(*iii*) Building under construction.	Non Current Asset	Fixed Assets — Capital work-in-progress

Q. 17. Distinguish between a Company's Balance Sheet and Firm's Balance Sheet. *(ISC 2017)*

Ans.

Basis of Distinction	*Company's Balance Sheet*	*Firm's Balance Sheet*
1. Format and Contents	Format and Contents of a Company's Balance Sheet must be in accordance with Schedule III Part I of Company's Act 2013.	There is no statutory format or prescribed contents for the Balance Sheet of a firm.
2. Figures of Previous Year	Figures of the previous year must also be given against each figure of current year.	Figures of the previous year are not required in the Balance Sheet of a firm.
3. Order of Permanence or Liquidity	Company's Balance Sheet is prepared in order of permanence.	Firm's Balance Sheet may be prepared in order of permanence or liquidity.
4. Vertical form or Horizontal form	Company's Balance Sheet is prepared in Vertical form.	Firm's Balance Sheet is generally prepared in horizontal form.

Q. 18. Distinguish between General Reserve and Reserve Fund. *(ISC Specimen Question Paper, 2018)*

Ans.

General Reserve	*Reserve Fund*
1. Amount available against reserve is used in the business.	1. Amount available against reserve fund is invested in outside securities.
2. It can be freely used for any purpose.	2. It is created for a specific purpose and can be used for that purpose only.
3. General Reserve is not represented by any corresponding asset.	3. Reserve Fund is represented by a corresponding asset.

Q. 19. List any four items that are shown under the sub-head 'Other Current Assets' in the Balance Sheet of a company prepared as per Schedule III of the Companies Act, 2013. *(I.S.C. 2020)*

[Ans. (*i*) Prepaid Exp. (*ii*) Dividend receivable. (*iii*) Interest accrued on Investments, and (iv) Advance Tax.]

PRACTICAL QUESTIONS

(Q. No. 1 to 24 are strictly in the serial order of illustrations)

Q. 1. On 1st April, 2019 *X* Ltd. has a debit balance of ₹3,00,000 in Reserves and Surplus as Balance of Statement of Profit & Loss. It earned a profit of ₹5,00,000 for the year ended 31st March, 2020. How would you show these items in the Balance Sheet and notes to accounts?

[Ans. ₹2,00,000 will be shown under 'Reserve and Surplus'.]

Q. 2. *Y* Ltd. has the following balances on 1st April, 2019 :

	₹
Securities Premium Reserve	6,00,000
Statement of Profit & Loss	4,00,000

During the year ended 31st March, 2020, it incurred a loss of ₹2,60,000. How would you show these items in the Balance Sheet and notes to accounts?

[Ans. ₹7,40,000 will be shown under 'Reserve and Surplus'.]

Q. 3. *Z* Ltd. has the following balances on 1st April, 2019 :

	₹
General Reserve	2,50,000
Capital Reserve	1,50,000
Statement of Profit & Loss	2,00,000

During the year ended 31st March, 2020, it incurred a loss of ₹7,10,000. Show how these items will appear in the Balance Sheet and notes to accounts?

[Ans. (₹1,10,000) will be shown under 'Reserve and Surplus'.]

Q. 4. Axis Ltd. has the following balances on 1st April, 2019 :

	₹
Statement of Profit & Loss	3,00,000
Debenture Redemption Reserve	5,00,000
General Reserve	7,00,000
Securities Premium Reserve	2,00,000

It earned a profit of ₹6,00,000 for the year ended 31st March, 2020. It decided to transfer ₹3,00,000 towards General Reserve and ₹2,50,000 towards Debenture Redemption Reserve.

Directors proposed a final dividend of ₹80,000.

Show how these items will appear in the Balance Sheet and notes to accounts.

[Ans. Reserve and Surplus ₹23,00,000; Contingent Liabilities ₹80,000.]

Q. 5. Operating Cycle and the period when payment is made is given below. How will you classify the liability?

Particulars	*(i)*	*(ii)*	*(iii)*	*(iv)*	*(v)*	*(vi)*
Operating Cycle (Months)	9	11	11	18	18	10
Expected Period when payment is made (Months)	12	12	13	20	16	12

[Ans. (*i*) Current*; (*ii*) Current; (*iii*) Non Current; (*iv*) Non Current; (*v*) Current; (*vi*) Current]

*A liability will be treated as Current if payment is made within 12 months.

Q. 6. Operating Cycle and the period when payment is received is given below. How will you classify the asset?

Particulars	*(i)*	*(ii)*	*(iii)*	*(iv)*	*(v)*	*(vi)*
Operating Cycle (Months)	10	10	10	15	15	20
Expected Period when payment is received (Months)	9	12	14	14	18	18

[Ans. (*i*) Current; (*ii*) Current*; (*iii*) Non Current; (*iv*) Current; (*v*) Non Current; *vi*) Current.]

*An asset will be treated as Current if payment is received within 12 months.

Q. 7. State the major heads under which the items appearing on the equity and iabilities side of a company's Balance Sheet are classified.

[Ans. (*i*) Shareholder's Funds; (*ii*) Share Application Money Pending Allotment; *iii*) Non-Current Liabilities; (*iv*) Current Liabilities.]

Q. 8. State the major heads under which the items appearing on the assets side of company's Balance Sheet are classified.

[Ans. (*i*) Non-Current Assets; (*ii*) Current Assets.]

Q. 9. How will you classify the following in a Company's Balance Sheet?

(*i*) Reserve and Surplus; (*ii*) Money received against share warrants.

[Ans. Both will be classified under 'Shareholder's Funds.]

Q. 10. Name the Sub-headings under which Current Liabilities shall be classified n a Company's Balance Sheet.

[Ans. Current Liabilities shall be classified as follows :

(*i*) Short-term borrowings
(*ii*) Trade payables
(*iii*) Other current liabilities
(*iv*) Short-term provisions]

Q. 11. Name the sub-headings under which Current Assets shall be classified in a ompany's Balance Sheet.

[Ans. Current Assets shall be classified as follows :

(*i*) Current investments
(*ii*) Inventories
(*iii*) Trade receivables
(*iv*) Cash and Bank Balance
(*v*) Short-term loans and advances
(*vi*) Other current assets]

Q. 12. Under what heads will you classify the following items on the equity & iability side of the Balance Sheet of a limited company : *(C.B.S.E. 2020)*

(*i*) Unclaimed Dividend
(*ii*) Proposed Dividend
(*iii*) Securities Premium Reserve
(*iv*) Share Forfeited Account

(*v*) Public Deposits

(*vi*) Debentures issued by the Company. *(C.B.S.E. 2020)*

Ans.

	Heading	*Sub-heading*
(*i*)	Current Liabilities	Other Current Liabilities
(*ii*)	Contingent Liabilities (in Notes to Accounts).	
(*iii*)	Shareholder's Funds	Reserves and Surplus
(*iv*)	Shareholder's Funds	It is added to 'Subscribed Capital'
(*v*)	Non-Current Liabilities	Long term Borrowings
(*vi*)	Non-Current Liabilities	Long-term Borrowings

Q. 13. Under what major heads the following items on the Assets side of the Balance Sheet of a Company will be presented : *(I.S.C. 2020)* *(C.B.S.E. 2020)*

(A) Marketable Securities

(B) Loose Tools

(C) Live Stock

(D) Goods in Transit

(E) Prepaid Expenses

Ans.

	Heading	*Sub-heading*
(A)	Current Assets	Current Investments
(B)	Current Assets	Inventories
(C)	Non-Current Assets	Fixed Assets — Tangible Assets
(D)	Current Assets	Inventories
(E)	Current Assets	Other Current Assets

Q. 14 (A). How would you disclose the following items in the Balance Sheet of a Limited Company?

(*i*) Outstanding Salary

(*ii*) Bank Balance

(*iii*) Unpaid matured deposits

(*iv*) Preliminary Expenses

(*v*) Bills Payable

Ans.

	Heading	*Sub-heading*
(*i*)	Current Liabilities	Other Current Liabilities
(*ii*)	Current Assets	Cash and Bank Balance
(*iii*)	Current Liabilities	Other Current Liabilities
(*iv*)	To be written off in the same year in which they occur.	
(*v*)	Current Liabilities	Trade Payables

Q. 14 (B). Under what heads the following items are shown in the Balance Sheet of a Company?

(*i*) Patents and Trade Marks (*I.S.C. 2020*)

(*ii*) Income Received in Advance

(*iii*) Debentures issued by the Company.

(*iv*) Stores and Spare-parts.

(*v*) Motor Vehicles (*C.B.S.E. 2020*)

(*vi*) Government Securities

(*vii*) Uncalled Liability on partly paid shares.

Ans.

	Heading	*Sub-heading*
(*i*)	Non Current Assets	Fixed Assets — Intangible Assets
(*ii*)	Current Liabilities	Other Current Liabilities
(*iii*)	Non-Current Liabilities	Long-term Borrowings
(*iv*)	Current Assets	Inventories
(*v*)	Non-Current Assets	Fixed Assets — Tangible Assets
(*vi*)	Non-Current Assets	Non-Current Investments
(*vii*)	Commitments in (Notes to Accounts).	

Q. 15. Under what heads the following are recorded in a Company's Balance Sheet?

I. Computer Software (*C.B.S.E. 2020*)

II. Bills Receivable

III. Interest Accrued and Due on Debentures

IV. Interest Accrued on Investments

V. Calls in Advance (*C.B.S.E. 2020*)

Ans.

	Heading	*Sub-heading*
I.	Non Current Assets	Fixed Assets — Intangible Assets
II.	Current Assets	Trade Receivables
III.	Current Liabilities	Other Current Liabilities
IV.	Current Assets	Other Current Assets
V.	Current Liabilities	Other Current Liabilities

Q. 16. Under what headings will you show the following items in the Balance Sheet of a Company :

(*i*) Credit Balance of Statement of Profit & Loss

(*ii*) Employees earned leave payable on retirement.

(*iii*) Provision for Provident Fund Scheme

(*iv*) Provision for Employee Benefits (to be settled within 12 months) (*C.B.S.E. 2020*) (*v*) Provision for Doubtful Debts

(*vi*) Contracts remaining to be executed

[**Ans.** (*i*) Shareholder's Funds under 'Reserve & Surplus'; (*ii*) Non Current Liabilities under 'Long term Provisions; (*iii*) Non Current Liabilities under 'Long term Provisions'; (*iv*) Current Liabilites under 'Short term Provisions'; (*v*) Current Assets — Deducted from Trade Receivables; (*vi*) Commitments (to be shown in Notes to Accounts)]

Q. 17. How will you show the following items in the Balance Sheet of a Company: *(C.B.S.E. 2020)*

(*i*) Stores and Spares
(*ii*) Debentures due for Redemption
(*iii*) Live Stock
(*iv*) Licences and franchise
(*v*) Advance from Customers
(*vi*) Advance to Suppliers
(*vii*) Commision Received in Advance

[**Ans.** (*i*) Current Assets under 'Inventories'; (*ii*) Current Liabilities under 'Other Current Liabilities'; (*iii*) Non Current Assets under 'Fixed Assets — Tangible Assets'; (*iv*) Non Current Assets under 'Fixed Assets — Intangible Assets'; (*v*) Current Liabilities under 'Other Current Liabilities; (*vi*) Current Assets under 'Short-term Loans and Advances' (*vii*) Current Liabilities under 'Other Current Liabilities'.]

Q. 18. The following balances have been extracted from the books of Robin Ltd. as on 31st March, 2022 :

	₹
Share Capital	10,00,000
Securities Premium	1,00,000
12% Debentures	5,00,000
Trade Payables	2,00,000
Provision for Taxation	50,000
Profit and Loss Statement (Dr.)	50,000
Livestock	9,00,000
Investment in Government Bonds	4,00,000
Work-in-progress	4,00,000
Preliminary Expenses	1,00,000
Patents	40,000
Unclaimed Dividend	10,000
Trade Receivables	20,000
Public Deposits	50,000

Prepare the Balance Sheet of the company as per Schedule III, Part I of the Companies Act, 2013.

[**Ans.** Total of Balance Sheet ₹17,60,000]

Hint : Work in Progress is shown as Inventory.

Q. 19. Following balances appeared in the books of Keshav Ltd. as at 31st March, 022. You are required to prepare a Balance Sheet in prescribed form :

	₹	₹
Share Capital (50,000 Shares of ₹10 each)		5,00,000
Preliminary Expenses	30,000	
Fixed Deposits accepted		10,000
Calls in arrears (On 1,000 Shares @ ₹2 each)	2,000	
Provident Fund		60,000
Premises	4,00,000	
Machinery	4,20,000	
Trade Receivables	2,40,000	
Trade Payables		75,000
Provision for Bad Debts		12,000
Bank Loan		4,50,000
Stock in Trade	1,50,000	
Prepaid Expenses	2,000	
Balance of Statement of Profit & Loss		2,10,000
Stores	40,000	
Loose Tools	15,000	
Cash at Bank	33,000	
Provision for Taxation		15,000
	13,32,000	13,32,000

The authorised capital of the company is ₹10,00,000 divided into 10,000 shares of ₹100 each.

[**Ans.** Balance Sheet Total ₹12,88,000.]

Hint. (*i*) Preliminary Expenses shall be written off from balance of Statement of Profit & Loss. (*ii*) Provision for Doubtful Debts will be deducted from trade receivables.

Q. 20. The following Balance Sheet is prepared by an amateur accountant. You are required to redraft it as per schedule III Part I of Companies Act 2013.

BALANCE SHEET

for the year ended 31st March, 2022

Liabilities	₹	*Assets*	₹
12% Debentures	2,00,000	Land and Buildings	7,80,000
Provision for Taxation	1,50,000	Stock in Trade	1,20,000
Securities Premium	50,000	Debtors	90,000
Investments in shares of Ravi Ltd.	11,20,000	Loose Tools	1,45,000
General Reserve	1,40,000	Cash and Bank	75,000
Creditors	1,00,000	Capital Redemption Reserve	11,20,000
Bills Payable	62,000	Leasehold Premises	6,00,000
Unclaimed Dividends	28,000	Preliminary Expenses	15,000
Balance of Statement of		Bills Receivable	2,00,000
Profit & Loss (Cr.)	70,000	Vehicles	2,75,000
Share Capital		Share Forfeiture	2,000
(15,000 Shares of ₹100 each)	15,00,000		

Calls in Arrears (on 500 Shares)	2,000		
	34,22,000		34,22,000

[Ans. Balance Sheet Total ₹34,05,000]

Q. 21. *X* Ltd. carried forward balance of ₹20,50,000 as surplus for the year ended on 31st March, 2021. During the year 2021-22 it made a profit of ₹71,80,000 before making provision for income tax. Provision for income tax is to be made for ₹30,00,000. Following appropriations were proposed by the Directors :

(*a*) Transfer ₹5,00,000 to the Dividend Equalisation Reserve.

(*b*) Pay the year's dividend on ₹5,00,000 10% cumulative Preference share capital.

(*c*) Pay 20% dividend on ₹60,00,000 Equity share capital.

(*d*) Pay ₹1,00,000 dividend to non-cumulative Preference Shares.

(*e*) Transfer ₹7,50,000 to Debenture Redemption Fund.

(*f*) Transfer 7.5% of Current year's net profit to General Reserve.

Ascertain the net amount of 'Surplus'.

[Ans. Current year Surplus ₹41,80,000; Net Surplus ₹46,66,500.]

Contingent Liability :	₹
Proposed Dividend on Cumulative Pref. Share Capital 10% on ₹5,00,000 =	50,000
Proposed Dividend on Equity Share Capital 20% on ₹60,00,000	12,00,000
Proposed Dividend on non-cumulative Pref. Share Capital	1,00,000
Total	13,50,000

Hint : (1) Transfer to General Reserve will be 7.5% of ₹41,80,000.

Q. 22. The following balances are left on the books of HMM Ltd. after its Profit and Loss Statement had been prepared for the year ended 31st March, 2022 :

Liabilities	₹	*Assets*	₹
Securities Premium	80,000	Plant and Equipment	6,60,000
General Reserve	1,00,000	Trade Receivables	1,20,000
Trade Payables	2,40,000	Cash at Bank	2,00,000
Share Capital paid up	8,00,000	Freehold Premises	5,50,000
(Nominal Capital – ₹10,00,000 in equity shares of ₹10 each)		Motor Vehicles	3,98,000
		Stock-in-Trade	2,67,000
		Prepaid Expenses	25,000
Net profit for the year as on 31.3.2022	6,00,000	Cash in Hand	40,000
Profit & Loss balance on 1.4.2021	1,40,000		
Accrued Expenses	3,00,000		
	22,60,000		22,60,000

You are required to draw up the company's Balance Sheet as at 31st March, 2022 after taking into account the following matters :

(*a*) Transfer ₹1,00,000 to General Reserve.

(*b*) Directors proposed a dividend of 12% on the paid up share capital.

[Ans. Net Surplus (after appropriations) ₹6,40,000; Total of Balance Sheet ₹22,60,000]

Note : Contingent Liability for Proposed Dividend ₹96,000.

Q. 23 The following are the balances of Ashok Photo Company Ltd., as at 31st March, 2022.

	₹
Securities Premium	40,000
Freehold Premises	2,50,000
Plant & Machinery	4,00,000
Furniture	15,300
Patents	4,200
Goodwill	1,20,000
Debtors	1,50,800
Share Capital : (40,000 shares of ₹10 each)	4,00,000
15% Debentures	1,00,000
Interest Accrued and due on Debentures	7,500
Creditors	95,100
Surplus (as on 1.4.2021)	2,80,000
Provision for Doubtful Debts	5,000
Debenture Sinking Fund	80,000
Bills Payable	25,500
Closing Inventories	1,26,000
Unsecured Loans : Public Deposits	50,000
Balances and Deposit with Excise authorities	16,000
Unclaimed Dividend	2,000
Net Profit for the year	1,48,000
Cash in Hand and at Bank	36,600
9% Government Securities	25,000
Underwriting Commission	9,200
Sinking Fund Investments	80,000

Informations:

(*i*) The authorised Capital of the Company is divided into 50,000 shares of ₹10 each.

(*ii*) Directors decided to transfer ₹38,000 to General Reserve.

(*iii*) Directors proposed a dividend of 12% on share capital.

Prepare the Balance Sheet of the Company as at 31st March, 2022 along with 'Notes to Accounts'.

[Ans. Net Surplus (after appropriations) ₹3,90,000; Total of Balance Sheet ₹12,18,900.]

Note : Contingent Liability for Porposed Dividend ₹48,000.

[illegible] The authorised capital of Avery Ltd. is ₹70,00,000 divided into 5,00,000 equity shares of ₹10 each and 2,00,000, 10% preference shares of ₹10 each. All the shares were issued and fully paid up. On 1st April, 2021 the company had a balance of profit ₹2,00,000 brought forward from the previous year. The net profit of the company for the year ended 31st March, 2022 amounted to ₹9,00,000.

The director's proposed to :

(*a*) transfer ₹1,00,000 to General Reserve;
(*b*) pay the dividend of 12% on equity shares;
(*c*) pay the year's dividend on preference shares;
(*d*) carry forward the remaining balance.

You are required to show how the items would appear in the Balance Sheet of the Company and prepare 'Notes to Accounts'.

[Ans. Net Surplus ₹10,00,000; Balance of 'Reserve and Surplus' ₹11,00,000; Balance Sheet Total ₹81,00,000.]

Note : Contingent Liability for Proposed Dividend 8,00,000.

ADDITIONAL QUESTIONS

Q. [illegible]. Under which major head/sub-head will the following items be presented in the Balance Sheet of a company as per Schedule III, Part I of the Companies Act, 2013?

(*i*) Computer software
(*ii*) Calls-in-advance
(*iii*) Outstanding salary
(*iv*) Securities Premium Reserve
(*v*) Patents
(*vi*) Interest accrued on Investment

(C.B.S.E. 2020; Chennai, Mumbai)

Items	*Major Head*	*Sub-Head*
(*i*) Computer software	Non-Current Assets	Fixed Assets-Intangible Assets
(*ii*) Calls in advance	Current Liabilities	Other Current Liabilities
(*iii*) Outstanding salary	Current Liabilities	Other Current Liabilities
(*iv*) Securities premium reserve	Shareholders funds	Reserves and Surplus
(*v*) Patents	Non-Current Assets	Fixed Assets-Intangible Assets
(*vi*) Interest accrued on investment	Current Assets	Other current Assets

Q. [illegible]. Under which heads and sub heads will the following items appear in the Balance Sheet of a company as per Schedule III Part I of the Companies Act 2013 :

(*i*) Loose Tools
(*ii*) Bills Receivable
(*iii*) Debentures issued by the Company
(*iv*) Patents

(From I.S.C. Guidelines, 2013)

Ans.

	Head	*Sub-head*
Loose Tools	Current Liabilities	Inventory
Bills Receivable	Current Assets	Trade Receivables
Debentures issued by the company	Non Current Liabilities	Long Term Borrowing
Patents	Non Current Assets	Fixed Assets-Intangible

Q. 27. From the following particulars of Ronald Ltd., prepare its Balance Sheet as at 31st March, 2013 (as per Schedule III of the Companies Act, 2013) along with Notes to Accounts :

	₹
Authorised Equity Share Capital (10,000 shares @ ₹10)	1,00,000
Authorised 6% Preference Share Capital (1,000 shares @ ₹100)	1,00,000
Issued Equity Share Capital (7,000 shares @ ₹10)	70,000
Issued 6% Preference Share Capital (1,000 shares @ ₹100)	1,00,000
Subscribed Equity Share Capital (5,000 shares, ₹8 called up, Calls in arrear ₹3 on 100 shares)	
Subscribed 6% Preference Share Capital (1,000 shares @ ₹100)	1,00,000
500, 5% Debentures of ₹1,000 each	5,00,000
Short-term loan from bank	10,000
Debtors	5,000
Provision for Doubtful Debts	200
Provision for Tax	1,000
General Reserve	4,000
Statement of P/L (Dr.)	6,000
Marketable Securities	500

(From I.S.C. Guidelines, 2013)

SOLUTION : EXTRACT OF BALANCE SHEET OF RONALD LTD.

as at 31st March, 2013

Particulars	*Note No.*	*31.3.2013* ₹	*31.3.2012* ₹
I. EQUITY AND LIABILITIES :			
(1) **Shareholders' funds**			
(*a*) Share capital	1	1,39,700	
(*b*) Reserves and surplus	2	(2,000)	
(2) **Non-Current Liabilities**			
Long-term Borrowings	3	5,00,000	
(3) **Current Liabilities**			
(*a*) Short-term Borrowings	4	10,000	
(*b*) Short-term Provisions	5	1,000	
TOTAL			
II. ASSETS :			
Current Assets			
(*a*) Current Investments	6	500	
(*b*) Trade Receivables	7	4,800	
TOTAL			

Notes to Accounts :

	Particulars		₹
(1)	**Share Capital :**		
	Authorised Capital		
	10,000 Equity shares of ₹10 each		1,00,000
	1,000 6% Preference shares of ₹100 each		1,00,000
			2,00,000
	Issued Capital		
	7,000 Equity Shares of ₹10 each		70,000
	1,000 6% Preference Shares of ₹100 each		1,00,000
			1,70,000
	Subscribed Capital		
	Subscribed and fully paid up		
	1,000 6% Preference shares of ₹100 each		1,00,000
	Subscribed but not fully paid up		
	5,000 equity shares of ₹10 each, ₹8 called up	40,000	
	Less : Calls-in-arrear	(300)	39,700
			1,39,700
(2)	**Reserves and Surplus :**		
	General Reserve	4,000	
	Statement of P & L	(6,000)	(2,000)
(3)	**Long-term Borrowings :**		
	500, 5% Debentures of ₹1,000 each		5,00,000
(4)	**Short-term Borrowings :**		
	Short-term loan from bank		10,000
(5)	**Short-term Provisions :**		
	Provision for Tax		1,000
(6)	**Current Investments :**		
	Marketable Securities		500
(7)	**Trade Receivables**		
	Debtors	5,000	
	Less : Provision for Doubtful Debts	200	4,800

Q. 28. Under which heads and sub heads will the following items appear in the Balance Sheet of a company as per Schedule III of the Companies Act, 2013 :

(*i*) Bills Receivable
(*ii*) Interest accrued and due on debentures
(*iii*) Trade Creditors
(*iv*) Provision for Taxation
(*v*) Stores and spares *(I.S.C. 2014)*

[Ans.

Item	*Heading*	*Sub-heading*
(*i*) Bills Receivable	Current Assets	Trade Receivables

(*ii*) Interest accrued and due on debentures	Current Liabilities	Other Current Liabilities
(*iii*) Trade Creditors	Current Liabilities	Trade Payables
(*iv*) Provision for Taxation	Current Liabilities	Shot term Provision
(*v*) Stores and Spares	Current Assets	Inventories

Q. [illegible]. From the given Trial Balance, prepare the Balance Sheet of Moonlight Limited as at 31st March, 2014.

TRIAL BALANCE *as at 31st March, 2014*

Date	*Particulars*	*L.F.*	*Dr.*	*Cr.*
			₹	₹
	Share Capital (40,000 Equity Shares of ₹10 each)			4,00,000
	Bills Receivable		90,000	
	16% Mortgage Loan			1,70,000
	Stores and Spares		1,15,000	
	Debtors		1,66,000	
	Plant and Machinery		2,90,000	
	Goodwill		40,000	
	Provision for Tax			26,000
	General Reserve			1,30,000
	Cash in Hand		18,000	
	Calls in Arrears (on 1,000 Shares)		2,000	
	Marketable Securities		5,000	
	Total		7,26,000	7,26,000

(ISC, 2015)

OLUTION : BALANCE SHEET OF MOONLIGHT LTD.

As at 31st March 2014

Particulars	*Note No.*	*Amount Current year*
I. EQUITY AND LIABILITIES :		₹
1. Shareholder's Funds :		
(*a*) Share Capital	1	3,98,000
(*b*) Reserves & Surplus	2	1,30,000
2. Non-Current Liabilities		
(*a*) Long-Term Borrowings	3	1,70,000
3. Current Liabilities		
(*a*) Short Term Provisions	4	26,000
Total		7,24,000
II. ASSETS :		
1. Non-Current Assets		
(*a*) Fixed Assets		
(*i*) Tangible Assets	5	2,90,000
(*ii*) Intangible Assets	6	40,000

2. Current Assets	7	5,000
(*a*) Current Investments	8	1,15,000
(*b*) Inventories	9	2,56,000
(*c*) Trade Receivables	10	18,000
(*d*) Cash & Bank Balance		
Total		7,24,000

Notes to Accounts :

Particulars			₹
1. **Share Capital**			
Authorised Capital			
..... Equity Shares of ₹10 each			
Issued Capital			
..... Equity Shares of ₹10 each			
Subscribed Capital			
Subscribed and Fully Paid			
39,000 Equity Shares of ₹10 each fully Called up		3,90,000	
Subscribed but Not Fully Paid			
1,000 Equity Shares of ₹10 each fully Called up	10,000		
Less : Calls in Arrears	2,000	8,000	3,98,000
2. **Reserves & Surplus**			
General Reserve			1,30,000
3. **Long-Term Borrowings**			
16% Mortgage Loan			1,70,000
4. **Short Term Provisions**			
Provision for Tax			26,000
5. **Tangible Assets**			
Building			2,90,000
6. **Intangible Assets**			
Goodwill			40,000
7. **Current Investment**			
Marketable Securities			5,000
8. **Inventories**			
Stores & Spares			1,15,000
9. **Trade Receivables**			
Debtors		1,66,000	
Bills Receivable		90,000	2,56,000
10. **Cash & Bank Balance**			
Cash in Hand			18,000

Q. 30. Under which heads and sub heads will the following items appear in the Balance Sheet of a company as per Schedule III of the Companies Act, 2013 :

(*i*) Trade Debtors
(*ii*) Marketable Securities
(*iii*) Finished Goods
(*iv*) Patents

(I.S.C. 2020)

[**Ans.**

	Item	Heading	Sub-heading
(*i*)	Trade Debtors	Current Assets	Trade Receivables
(*ii*)	Marketable Securities	Current Assets	Current Investments
(*iii*)	Finished Goods	Current Assets	Inventory
(*iv*)	Patents	Non-Current Assets	Fixed Assets (intangible)

Q. 31. Xylo Ltd. was formed on 1st April, 2017, with an authorized capital of ₹12,00,000 divided into Equity Shares of ₹10 each. It issued a prospectus inviting applications for 30,000 shares to be issued at par. The issue was fully subscribed and the amount due on the shares was received by the company.

On 1st April, 2018, the company issued another 60,000 shares at a premium of ₹2 per share to be received with allotment. Applications for 55,000 shares were received which were duly allotted.

All the amounts due on these shares were received except the final call of ₹2 per share on 1,000 shares.

On 1st October, 2018, the company also issued 2,000 *6% debentures of ₹100 each* at par, to be redeemed at par in *five equal annual instalments* beginning from 1st October, 2019. The entire issue price of these debentures was received by the company with application.

Half yearly interest on the debentures of ₹6,000 was paid by the company to the debenture holders on 31st March, 2019.

You are required to show the relevant items under :

(*i*) Equity and Liabilities in the Balance Sheet of the Company as at 31st March, 2019 (prepared as per Schedule III of the Companies Act, 2013).

(*ii*) Notes to Accounts. *(I.S.C. 2020)*

SOLUTION : BALANCE SHEET OF XYLO LTD.

as at 31st March, 2019

Particulars	*Note No.*	*31.3.2019*
I. EQUITY AND LIABILITIES :		₹
1. **Shareholder's Funds :**		
(*a*) Share Capital	1	8,48,000
(*b*) Reserve and Surplus	2	1,04,000
2. **Non-Current Liabilities :**		
Long-term Borrowings	3	1,60,000
3. **Current Liabilities :**		
Other Current Liabilities	4	40,000

Notes to Accounts :

		₹
(1) **Share Capital :**		
Authorized Capital		
1,20,000 Equity Shares @₹10 each		12,00,000
Issued Capital :		
90,000 Equity Shares @₹10 each		9,00,000
Subscribed Capital :		
Subscribed and fully paid		
84,000 Equity Shares @₹10 each		8,40,000
Subscribed but not fully paid		
1,000 Equity Shares @₹10 each	10,000	
Less : Calls-in-arrears	(2,000)	8,000
		8,48,000
(2) **Reserve and Surplus :**		
Securities Premium Reserve		1,10,000
Balance of Statement of Profit & Loss (interest on debentures)		(6,000)
		1,04,000
(3) **Long-term Borrowings :**		
1,600, 6% Debentures of ₹100 each		1,60,000
(4) **Other Current Liabilities :**		
Current Maturity of Long-term Debt		
400, 6% Debentures of ₹100 each		40,000

Multiple Choice Questions

Choose the Best Alternate :

Q. 1. The Balance Sheet provides information about financial position of an enterprise :

(A) Over a period of time
(B) During a period of time
(C) For a period of time
(D) At a point of time

(C.B.S.E. 2020; Delhi)

Q. 2. Balance sheet of a company is required to be prepared in the format given in ....

(A) Schedule III Part II
(B) Schedule III Part I
(C) Schedule III Part III
(D) Table A

Q. 3. As per Companies Act, the Balance Sheet of a company is required to be presented in ....

(A) Horizontal Form
(B) Vertical Form
(C) Either Horizontal or Vertical Form
(D) Neither of the above

Q. 4. Which of the following is not required to be prepared under the Companies Act?

(A) Statement of Profit and Loss (B) Balance Sheet
(C) Report of Director's and Auditor's (D) Funds Flow Statement

Q. 5. According to prescribed order of assets in a Company's Balance Sheet .... assets should be shown first of all.

(A) Non-Current Assets (B) Current Assets
(C) Current Investments (D) Loans and Advances

Q. 6. In a Company's Balance Sheet .... appear under the head 'non-current assets'.

(A) Goodwill (B) Patents
(C) Vehicles (D) All of the above

Q. 7. Calls in Arrears appear in a Company's Balance Sheet under ....

(A) Reserve & Surplus (B) Shareholder's Funds
(C) Contingent Liabilities (D) Short-term Borrowings

Q. 8. Calls in advance appear in a Company's Balance Sheet under ....

(A) Share Capital
(B) Current Liability
(C) Share Application money pending allotment
(D) Reserve & Surplus *(C.B.S.E. 2020; Punjab)*

Q. 9. Short-term Borrowings appear in a Company's Balance Sheet under the head ....

(A) Current Assets (B) Current Liabilities
(C) Non-Current Liabilities (D) Non-Current Assets

Q. 10. Public Deposits appear in a Company's Balance Sheet under :

(A) Intangible Assets (B) Current Liabilities
(C) Long-term Provisions (D) Long-term Borrowings
(C.B.S.E. 2020; Rajasthan)

Q. 11. Goodwill appears in a Company's Balance Sheet under the Sub-head ....

(A) Unamortized Assets (B) Non-Current Investment
(C) Intangible Assets (D) Tangible Assets

Q. 12. 'Loose Tools' appear in the company's Balance Sheet under the head/sub-head :

(A) Inventory (B) Non-Current Assets
(C) Other Current Assets (D) Stores and Spare Parts
(C.B.S.E. 2020; Rajasthan)

Q. 13. Share Forfeiture Account appears in a Company's Balance Sheet under the sub-head ....

(A) Share Capital (B) Reserve and Surplus
(C) Other Long-term Liabilities (D) Other Current Liabilities
(C.B.S.E. 2020; Chennai, Kolkata)

Q. 14. Expenses allowed on issue of shares appears in a Company's Balance Sheet under :

(A) Share Capital (B) Current Liability

(C) Unamortized Expenditure (D) Contingent Liability

Q. 15. Securities Premium Reserve appears in a Company's Balance Sheet under :

(A) Share Capital (B) Long-term Provision

(C) Short-term Provision (D) Reserve & Surplus

Q. 16. Prepaid Expenses appear in a Company's Balance Sheet under the Sub-head ....

(A) Other Current Assets (B) Short-term Loans & Advances

(C) Intangible Assets (D) Other Non-Current Assets

Q. 17. .... appear in a Company's Balance Sheet under the Sub-head Short-term Provision.

(A) Interest Accrued but not due on Borrowings

(B) Provision for Tax

(C) Unpaid Dividend

(D) Calls in Advance

Q. 18. Provision for Tax appears in a Company's Balance Sheet under the Sub-head.............. .

(A) Short-term Provisions (B) Reserves and Surplus

(C) Long-term Provisions (D) Other Current Liabilities

Q. 19. Bills Receivables appear in a Company's Balance Sheet under the Sub-head ....

(A) Current Investments (B) Cash Equivalents

(C) Trade Receivables (D) Short term Loans and Advances

Q. 20. Trade Investments appear in a Company's Balance Sheet under the Sub-head ....

(A) Current Investments (B) Non-Current Investments

(C) Intangible Assets (D) Short-term Loans and Advances

Q. 21. 'Claims against the Company **not** acknowledged as debts' is shown under the head ....

(A) Current Liabilities (B) Non-Current Liabilities

(C) Commitments (D) Contingent Liabilities

Q. 22. Unclaimed dividend appears in a Company's balance Sheet under the Sub-head ....

(A) Short-term Borrowings (B) Trade Payables

(C) Other Current Liabilities (D) Short-term Provisions

(C.B.S.E. 2020; Kerala)

Q. 23. Interest accrued and due on debentures appear in a Company's Balance Sheet under the Sub-head ....

(A) Short-term Borrowings (B) Trade Payables

(C) Other Current Liabilities (D) Short-term Provisions

Q. 24. Interest accrued but **not** due on loans appear in a Company's Balance Sheet under the Sub-head ....

(A) Short-term Borrowings (B) Trade Payables
(C) Other Current Liabilities (D) Short-term Provisions

Q. 25. 6% Debentures appear in a Company's Balance Sheet under the Sub-head ....

(A) Long-term Provisions (B) Long-term Borrowings
(C) Other Current Liabilities (D) Other Long-term Liabilities

Q. 26. Interest accrued on Investments appear in a Company's Balance Sheet under the Sub-head ....

(A) Non-Current Investments (B) Current Investments
(C) Other Current Assets (D) Other Non-Current Assets

Q. 27. 'Accumulated Dividend Arrears' on preference shares is shown in the Company's Balance Sheet as

(A) Current Liability (B) Contingent Liability
(C) Commitments (D) Short-term Provision

Q. 28. 50,000, 9% Debentures redeemable within 12 months of the date of Balance Sheet will be shown under :

(A) Short-term Borrowings (B) Short-term Provision
(C) Other Current Liability (D) Trade Payables

Q. 29. Which one of the following is Commitment?

(A) Proposed Dividend
(B) Interim Dividend
(C) Unpaid/Unclaimed Dividend
(D) Dividend Arrears on Cumulative Preference Shares

Q. 30. Which of the following items is shown under the head 'Current Assets' while preparing the Balance Sheet of a company?

(A) Trade Investment (B) Underwriting Commission
(C) Inventories (D) Livestock

Q. 31. While preparing the Balance Sheet of a company 'Underwriting Commission' is shown under which head?

(A) Unamortized Expenditure (B) Current Assets
(C) Non-Current Assets (D) Current Liability

Q. 32. Which of the following items is shown under the head 'Current Liabilities' while preparing the Balance Sheet of a company?

(A) Securities Premium Reserve (B) Debentures
(C) Livestock (D) None of the above

Q. 33. While preparing the Balance Sheet of a company 'Securities Premium' is shown under :

(A) Current Liability (B) Share Capital
(C) Long-term Borrowings (D) None of the above

Q. 34. Which of the following items is shown under the head 'Non-Current Assets' while preparing the Balance Sheet of a company?

(A) Underwriting Commission
(B) Current Investment
(C) Inventory
(D) Patents

Q. 35. Under which heading the item 'Bills Discounted but not yet matured' will be shown in the Balance Sheet of a company?
(A) Current Liability
(B) Current Assets
(C) Contingent Liabilities
(D) Unamortized Expenditure

Q. 36. Which one of the following items is shown under the heading 'current liabilities' in the Balance Sheet of a company?
(A) Investments
(B) Reserve Fund
(C) Unclaimed Dividend
(D) Livestock

Q. 37. Which one of the following is **not** presented under 'Current Liabilities' in the Balance Sheet of a company?
(A) Short-term Borrowings
(B) Deferred Tax Liabilities
(C) Short-term Provisions
(D) Trade Payables

(I.S.C. Sample Paper 2021)

Q. 38. While preparing the Balance Sheet of a Company which item is shown under the head 'Long term Borrowings'?
(A) 6% Debentures
(B) Security Premium Reserve
(C) Trade Payables
(D) None of the above

Q. 39. Share Capital of a Company consists of 5,00,000 Shares of ₹10 each, ₹8 called up. All the shareholders have duly paid the called up amount. Share capital will be shown as :
(A) Subscribed and Fully Paid
(B) Subscribed but not Fully Paid
(C) Both A and B
(D) None of the above

Q. 40. A Company has issued 2,00,000 Equity Shares of ₹10 each and it has called the entire nominal value of the share. It has received the entire amount except final call of ₹3 per share on 5,000 shares. Subscribed Capital will be shown as follows:

(A) Subscribed and fully paid		
2,00,000 Equity Shares of ₹10 each	20,00,000	
Less : Call in Arrears	15,000	19,85,000

(B) Subscribed but not fully paid		
2,00,000 Equity Shares of ₹10 each	20,00,000	
Less : Call in Arrears	15,000	19,85,000

(C) Subscribed and fully paid		
1,95,000 Equity Shares of ₹10 each		19,50,000
Subscribed but not fully paid		
5,000 Equity Shares of ₹10 each	50,000	
Less : Call in Arrears	15,000	35,000
		19,85,000

(D) Can be shown as (B) or as (C)

Q. 41. Change in Inventories means :

(A) Opening Inventories *less* Closing Inventories

(B) Closing Inventories *less* Opening Inventories

(C) Difference between Opening Inventories and Closing Inventories, if Opening Inventories are higher

(D) Difference between Closing Inventories and Opening Inventories, if Closing Inventories are higher.

Q. 42. Which of the following is **not** a sub-head under the Current Assets?

(A) Cash and Cash Equivalents
(B) Trademarks
(C) Short-term Loans and Advances
(D) Inventories

(C.B.S.E. 2020; Kolkata, Lucknow)

Q. 43. 'Security Deposits' are presented in the Balance Sheet of the company under the sub-head :

(A) Other Non-Current Assets
(B) Long-term Loans and Advances
(C) Fixed Assets
(D) Other Current Liabilities

(C.B.S.E. 2020; Kolkata, Lucknow)

Q. 44. Which of the following is **not** a part of Finance Cost (in statement of profit and loss)?

(A) Bank Charges
(B) Interest Paid on Debentures
(C) Interest Paid on Public Deposits
(D) Loss on Issue of Debentures

(C.B.S.E. Sample Paper, 2020)

Q. 45. If the operating cycle of a company cannot be identified, it is assumed to be:

(A) 18 months
(B) 12 months
(C) 10 months
(D) 15 months

(I.S.C. Sample Paper, 2021)

Q. 46. A company has an operating cycle of eight months. It has accounts receivables amounting to ₹1,00,000 out of which ₹60,000 have a maturity period of 11 months. How would this information be presented in the balance sheet?

(A) ₹40,000 as current assets and ₹60,000 as non-current assets.

(B) ₹60,000 as current assets and ₹40,000 as non-current assets.

(C) ₹1,00,000 as non-current assets.

(D) ₹1,00,000 as current assets. *(C.B.S.E. Sample Paper, 2021)*

Q. 47. Match the items given in Column I with the headings/subheadings (Balance sheet) as defined in Schedule III of Companies Act 2013.

Column I	*Column I*
(I) Loose Tools	(*a*) Intangible Fixed Assets
(II) Patents	(*b*) Other Current Assets
(III) Prepaid Insurance	(*c*) Long term Borrowings
(IV) Debentures	(*d*) Inventories
(V) Machinery	(*e*) Tangible Fixed Assets

Choose the correct option :

A. (I)-(*a*), (II)-(*b*), (III)-(*d*), (IV)-(*c*), (V)-(*e*)
B. (I)-(*d*), (II)-(*a*), (III)-(*b*), (IV)-(*c*), (V)-(*e*)
C. (I)-(*d*), (II)-(*a*), (III)-(*b*), (IV)-(*e*), (V)-(*c*)
D. (I)-(*e*), (II)-(*d*), (III)-(*a*), (IV)-(*b*), (V)-(*b*)

(C.B.S.E. Sample Paper, 2021)

(See Answers at the end of the book.)

10

Financial Statements Analysis

Meaning of Financial Statement Analysis

Financial statements present a mass of complex data in absolute monetary terms and reveal little about the liquidity, solvency and profitability of the business. In financial analysis, the data given in financial statements is classified into simple groups and a comparison of various groups is made with one another to pin-point the strong points and weaknesses of a business. For instance, if all items relating to current assets are placed in one group while all items relating to current liabilities are placed in another group, the comparison between the two groups will provide useful information. Actually the figures given in financial statements do not speak anything themselves. The analysis of these figures helps the interested reader by giving tongue to these mute heaps of figures.

In the words of Finney and Miller :

"Financial analysis consists in separating facts according to some definite plan, arranging them in groups according to certain circumstances and then presenting them in a convenient and easily read and understandable form."

In the words of John N. Myres :

"Financial statement analysis is largely a study of relationships among the various financial factors in a business, as disclosed by a single set of statements and a study of the trends of these factors as shown in a series of statements."

On the basis of above mentioned definitions, the main features of financial analysis are :

(1) To present the complex data contained in financial statements in simple and understandable form.

(2) To classify the items contained in financial statements in convenient and rational groups.

(3) To make comparisons between various groups to draw various conclusions.

Types or Methods of Financial Statement Analysis

Financial Statement Analysis can be of following types :

(*i*) **External Analysis :** This analysis is made by the parties who are outsiders for the business. These parties are investors, banks, financial institutions, creditors, government agencies, researchers etc. These parties do not have access to the detailed internal records of the business and hence their analysis is based almost entirely on published financial statements. The objective of such analysis varies from party to party and serves only a limited purpose.

(*ii*) **Internal Analysis :** This analysis is made by the persons who have access to the detailed internal records of the business. Such an analysis can, therefore, be performed by executives of the organisation. The main objective of such analysis is to assist the management in taking appropriate financial decisions.

(*iii*) **Horizontal (or Dynamic) Analysis :** In such type of analysis, financial statements for a number of years are reviewed and analysed. Hence, it is a time series analysis. Figures for two or more years are contained in such type of analysis and these figures are placed side-by-side to facilitate comparison. Such analysis indicates the increase or decrease in these items not only in absolute figures but also in percentage form. Thus, it involves making comparisons and establishing relationship among related items of an enterprise for a number of years. When data about sales, cost of production, profits etc. are compared for two or more years of a firm, they indicate the areas of strength and weakness of the enterprise. It also helps in knowing the trend of the business. Since such type of analysis is based on the data from year-to-year rather than only one year, it is also called '**Dynamic Analysis**'.

(*iv*) **Vertical (or Static) Analysis :** In such type of analysis, financial statements for a single year or on a particular date are reviewed and analysed with the help of proper devices like ratios. Hence, it is a cross-sectional analysis. It involves a study of the quantitative relationship among various items of Balance Sheet or Statement of Profit & Loss of a single period. The items in the financial statement are expressed as a percentage to total and the total is taken as equivalent to 100. Statements containing such analysis are termed as 'Common Size Statements'.

The Common Size Statement of Profit & Loss shows each element of Cost as a percentage of sales. It helps in analysing costs and operating results of the year. Similarly, in a common size Balance Sheet various assets can be expressed as percentage of total assets.

Since such type of analysis is based on the data of a single year, it is also called '**Static Analysis**'. Vertical analysis is useful in comparing the performance of several companies in the same group or departments in the same company.

Vertical analysis is not very useful for a proper analysis of the company's financial position because it depends on the data of a single period whereas the business is a dynamic process. In comparison to vertical analysis, the horizontal analysis is more useful because it brings out more clearly the nature and trends of current changes affecting the enterprise. Horizontal presentation emphasises the fact that statement for a series of periods are far more significant than those for a single period and that the accounts for one period are but an instalment of what is essentially a continuous history.

Distinction between Horizontal Analysis and Vertical Analysis

Basis	*Horizontal Analysis*	*Vertical Analysis*
1. **Period**	It requires financial statements of two or more accounting periods.	It requires financial statements of one accounting period.
2. **Items**	It involves a study of same items of different periods.	It involves a study of different items of same period.
3. **Information**	It provides information in absolute and percentage form.	It provides information in percentage form.

4.	**Usefulness**	It is usually used for Time Series Analysis.	It is usually used for Cross-Sectional Analysis.
5.	**Method**	This analysis can be done by preparing Comparative Balance Sheet and Comparative Statement of P & L.	This analysis can be done by preparing Common Size Balance Sheet, Common Size Statement of P & L and accounting ratios.

Intra-Firm Analysis : Intra-firm analysis is a comparison of financial variables of an enterprise for two or more accounting periods. It is also called 'Time Series Analysis' or 'Trend Analysis'.

Inter-Firm Analysis : Inter-firm analysis is a comparison of financial variables of two or more enterprises for the same accounting period to determine their competitive position. It is also called 'Cross-Sectional Analysis'.

Objectives or Purpose of Financial Analysis

The purpose of financial analysis depends on the needs of the person who is analysing these statements. These varying needs may be :

(1) **To Measure the Earning Capacity or Profitability :** According to **Robert Anthony**, "The overall objective of a business is to earn a satisfactory return on the funds invested in it, consistent with maintaining a sound financial position." Financial analysis helps in ascertaining whether adequate profits are being earned on the capital invested in the business. It is also disclosed by analysis of financial statements whether these profits are increasing or decreasing over the years. For this purpose, the financial statements of a few years are taken into account to compute the change in profits over the years. Such analysis helps in ascertaining the future profitability or earning capacity of the business.

(2) **To Measure the Solvency :** It can be ascertained from financial analysis whether the business is in a position to pay its short-term and long-term liabilities in time. For example, the liquidity ratios (current ratio and quick ratio) are calculated to ascertain whether the business enterprise has sufficient liquid funds to meet its short term liabilities and Debt Equity Ratio is calculated to ascertain whether the business enterprise has got the ability to repay the long term liabilities.

(3) **To Measure the Financial Strength :** The purpose of financial analysis is to assess the financial potential of the business. Analysis helps in providing answers to the following questions :

(*i*) Funds required for the purchase of new machinery and equipments will be available from internal resources of the business or not?

(*ii*) Based on the current reputation of the business, how much funds can be raised from external sources?

(4) **To Make Comparative Study with other Firms :** The purpose of financial analysis is to help the management to make a comparative study of the profitability of various firms engaged in same trade. Such comparison helps the management to study the position of their firm in respect of sales, expenses, profitability and working capital etc. in comparison to other firms.

(5) **To Measure the Capability of Payment of Interest and Dividend :** The purpose of analysis is to assess whether the firm will have sufficient profits to pay the

amount of interest in time and whether it has the capacity to pay the dividend in future at a higher rate. Analysis also indicates the number of times the profit is in comparison to interest. Analysis further indicates the extent to which the profit of the firm may decrease without in any way affecting its ability to meet interest and dividend obligations.

(6) **To Identify the Trend of the Business :** When data about sales, cost of production, profits etc. are compared for two or more years of a firm, they indicate the direction in which a business is moving. If sales are increasing continuously along with increase in profit margins, it is an indication of a healthy growth trend of the business. Such analysis helps in ascertaining whether the business is progressive or not.

(7) **To Judge the Efficiency of Management :** The purpose of financial analysis is to judge that the financial policies adopted by the management are proper or not. For example, if the actual ratios calculated on the basis of financial statements are in accordance with their standard ratios, the policies of the management may be said to be proper and efficient.

(8) **To Provide Useful Informations to the Management :** The object of financial analysis is to find out the shortcomings of the business, so that the management can take remedial measures to remove those shortcomings.

Uses of Financial Analysis :

Financial analysis can be used to take variety of decisions in the following areas :

(1) **For taking Investment Decisions :** Analysis of financial statements helps an investor to know whether the firm is fulfilling his expectations regarding the payment of dividend, appreciation in the value of investments made by him and safety of his investment. It helps him to take decision about continuation or discontinuation of his investment in the firm.

(2) **For taking Credit Decisions :** Analysis of financial statements is useful in making a decision whether to grant or extend credit to a customer.

(3) **For taking Dividend Decisions :** Such analysis is useful in deciding about how much portion of the profit is to be distributed as dividend and how much to retain.

(4) **For Estimating Trend of the Business :** Analysis of financial statements for a number of years reveals the trend of costs, sales, profits etc. It helps in assessing the future growth potential of the firm.

(5) **For Taking Various Managerial Decisions :** Analysis of financial statements discloses the liquidity, solvency and profitability of the business enterprise. It helps in locating the weak spots of the business. Such information enables the management to take various decisions.

Significance or Importance of Financial Analysis
Or
Parties Interested in Financial Analysis

At present, the analysis of financial statements has become of general interest. Various parties have become interested in the financial statements of a company due to various reasons. Different persons look at the same financial statement from different angles, *i.e.*, there are different users of financial statements, all of them using the same statement but for a different purpose. For example, a shareholder would be interested in the profitability whereas a short-term creditor would be concerned about the liquidity, *i.e.*, the firm's ability to pay its current liabilities. Therefore, the significance of the financial statement analysis may be studied from the point of view of various parties as follows :

(1) **Significance for Management :** Management of a firm is always interested in the solvency, profitability and the capital structure of the firm. They want to make sure that the business must be in a solvent position to pay the debts as and when they fall due. Similarly, they are interested not only in the current years' profit but also in the capacity of the business to earn more profits in future. By comparing the financial statements of their business with the financial statements of other firms in the same trade managements can draw significant conclusions about the sales, profits, expenses etc. In the words of **Gerstenberg :**

"The management can measure the effectiveness of its own policies and decisions, determine the advisability of adopting new policies and procedures and document to owners, the results of their managerial efforts."

(2) **Significance for Investors :** Investors and shareholders of the business are interested in the longevity of the business enterprise and therefore, they want to know the earning capacity of the business and its prospects for future growth and prosperity. Analysis of financial statements of a company helps them a great deal in assessing the capacity of the business to pay dividend at a higher rate and also the safety of their investments.

(3) **Significance for Creditors :** There are two types of creditors, (*i*) Short-term creditors, and (*ii*) Long-term creditors.

(*i*) Short-term creditors want to know the liquidity of the business, *i.e.*, to know whether the company will have sufficient current assets and cash to pay their debts or not. Current ratio and quick ratio calculated on the basis of financial statements help them in assessing this.

(*ii*) Long-term creditors want to know two things namely : (1) Whether the company will be able to pay the interest consistently, and (2) Whether the company will be able to pay their debts when they fall due. On the basis of interest coverage ratio they can ascertain whether the company will be able to pay the interest regularly or not and on the basis of debt-equity ratio they can ascertain whether the company will be able to pay their debts on maturity.

(4) **Significance for Government :** Government can judge on the basis of analysis of financial statements, which industry is progressing on the desired lines and which industry needs the financial help. Government can take a decision to reduce the GST in those industries where the profit margins are low in comparison to the cost of production. On the contrary, if the profit margins are too high in comparison to the cost of production, Government can increase the GST or can enforce the price regulations.

(5) **Significance for Financial Institutions :** All the financial institutions which provide finance to the industries such as Banks, Insurance companies, Unit Trust etc. want to know the profit earning capacity of the business and its long-term solvency. They want to assess not only the present position of the business enterprise but also its

likely position in the future. Analysis of financial statements helps them in ascertaining this.

(6) **Significance for Employees :** Analysis of financial statements helps the employees in determining the profitability of the business enterprise. They can ascertain as to how much bonus and increase in their wages is possible from the profits of the company. Analysis of financial statements also helps the trade unions in negotiating wages agreements.

(7) **Significance for Stock Exchange Authorities :** They analyse the financial statements of a company to determine its price earning ratio and earning per share (E.P.S.). With the help of such analysis, the market price of a company's share is determined.

(8) **Significance for Taxation Authorities :** They analyse the financial statements of a company to know whether the financial statements have been prepared in accordance with the legal provisions and whether the figures of production, sales and profits are correct for the purpose of assessment of GST and income tax etc.

(9) **Significance for Researchers :** Analysis of financial statements of a company is of much importance to a researcher who is conducting research in respect of the profitability, efficiency, financial soundness and future growth potential of that company.

(10) **Significance for Other Parties :** Some other parties may also be interested in the analysis of financial statements of a company from their own point of view, such as, economists, trade associations, consumer organisations etc.

Limitations of Financial Analysis

Financial analysis helps the interested parties to make an assessment of the earning capacity and financial soundness of a business enterprise. But such analysis has its own limitations. Such limitations should be kept in mind while using the informations provided by the financial analysis. Some of the limitations are as follows :

(1) **Limitations of Financial Statements :** Financial analysis is based on financial statements. But financial statements themselves suffer from certain limitations, hence the limitations of financial statements are also the limitations of their analysis. For example, (*i*) Sometimes the informations given in financial statements are incomplete and unauthentic, (*ii*) Financial Statements are based on accounting concepts and conventions. As such, the utility of financial analysis is decreased due to the shortcomings of financial statements.

(2) **Affected by Window-dressing :** Some firms resort to window-dressing their financial statements to cover up bad financial position on the eve of accounting date. For example, they may not record the purchases made at the end of the year or they may overvalue their closing stock. In such cases, the results obtained by analysis of financial statements will be misleading.

(3) **Do not Reflect Changes in Price Level :** Figures given in financial statements do not show the effect of changes in price level. As such, the comparison of past year figures with current year figures may lead to misleading conclusions. For example, if in 2019 a firm sells 10,000 metre of cloth for ₹10 lac and the same firm in 2020 sells the same type of 10,000 metre of cloth for ₹15 lac, it discloses an increase of 50% in

sales, whereas, in actual, the sales have not increased at all. As such, sufficient adjustments must be made for changes in price level before making the analysis.

(4) **Different Accounting Policies :** If two firms adopt different accounting policies, the comparison between the two will be unreliable. For example, one firm may provide depreciation on original cost method, whereas the other firm may adopt the written-down value method for providing the depreciation. Similarly, the method of valuation of closing stock may also differ from one firm to another. The results obtained from the comparison of the financial statements of such firms may give misleading picture.

(5) **Effect of Personal Ability and Bias of the Analyst :** Figures given in financial statements do not speak by themselves, hence, any conclusion can be drawn from these figures. Conclusions obtained from the analysis of these figures are affected to a great extent by the personal ability and knowledge of the analyst. For example, for calculating 'return on capital' one analyst may consider the profits after taxes, whereas, the other analyst may consider the profits before taxes. Similarly, the term 'Capital' may mean only the 'Shareholder's Funds' for one analyst, whereas the other analyst may take the 'Shareholder's Funds and Long Term Debts' as capital.

(6) **Difficulty in Forecasting :** Financial statements are a record of past events and historical facts. In the fast changing and developing modern business, the analysis of past information may not be of much use in future forecasting. Continuous changes take place in the demand of the product, policies adopted by the firm, the position of competition etc. As such, no estimate based on the analysis of historical facts can be made for future.

(7) **Lack of Qualitative Analysis :** Financial statements record only those events and transactions which can be expressed in terms of money. Qualitative aspects of business units are omitted from the books at all as these cannot be expressed in monetary terms. Thus, changes in management, reputation of the business, cordial management-labour relations, firm's ability to develop new products, efficiency of management, satisfaction of firm's customers etc. which have a vital bearing on the profitability of the company are all ignored and omitted from being recorded because all of these are qualitative in nature.

(8) **Limited Use of Single Year's Analysis of Financial Statements :** Results obtained from financial analysis assume significance only when compared with the figures of previous periods. For example, the profit of a firm to sales is 12%, whether this is satisfactory or not will depend upon the figures of previous years. If the firm earned 10% of sales as profit in the previous year, it may be considered to have done better this year. However, the financial statements of two years may not be comparable due to the changes in accounting policies.

It is clear from the above mentioned limitations that the results obtained from analysis of financial statements should not be taken as the true indicators of the strength and weaknesses of the concern. The results obtained from analysis must be read carefully and cautiously. The limitations of analysis must be kept in mind while taking decisions based on the results obtained from such analysis.

Short Answer Questions

Q. 1. What is meant by 'Financial Analysis'?

Ans. Financial analysis is a systematic process of classifying the data into simple groups and making a comparison of various groups with one another to pin-point the strong points and weaknesses of the business.

Q. 2. List any one objective of analysing the financial statements.

Ans. To measure the earning capacity of the business.

or

To measure the short-term and long-term solvency of the enterprise.

Q. 3. What is Horizontal Analysis?

Ans. When financial statements for a number of years are analysed, the analysis is called horizontal analysis. Such analysis is mostly in the form of 'Comparative financial statements'.

Q. 4. What is Vertical Analysis?

Ans. When financial statements for a single year are analysed, the analysis is called vertical analysis. The items in the financial statement are expressed as a percentage to total and the total is taken as equivalent to 100. Statements containing such analysis are termed as 'Common Size Statements'.

Q. 5. List any two uses of analysing the financial statements.

Ans.
1. Helpful in taking investment decisions.
2. Helpful in taking credit decisions.

Q. 6. Give one limitation of financial analysis.

Ans. Do not reflect price level changes.

or

Comparison is unreliable if different firms adopt different accounting policies.

Q. 7. What is the interest of shareholders or Investors in the analysis of financial statements?

Ans. (*i*) They want to judge the present and future earning capacity of the business
(*ii*) They want to judge the safety of their investment.

Q. 8. State the interest of tax authorities in the analysis of financial statements.

Ans. (1) To judge whether the financial statements have been prepared in accordance with the legal provisions.
(2) To judge whether various types of taxes have been paid appropriately.

Q. 9. What is the interest of lenders or Bankers in the analysis of financial statements?

Ans. (*i*) To judge the financial soundness of the business to repay their debts at maturity.
(*ii*) To judge that the enterprise has sufficient profits so as to make payment of interest regularly throughout the term of loan.

Q. 10. Give two areas of interest for management while analysing the financial statements.

Ans. (*i*) To know the profitability of the business enterprise.

(*ii*) To know the short-term and long-term solvency position of the enterprise.

Q. 11. How can the financial strength of a business enterprise be judged?

Ans. The financial strength of a business enterprise can be judged on the basis of

(*i*) its earning capacity, *i.e.*, profitability, and

(*ii*) its ability to repay the loans and pay dividends.

Q. 12. How the 'solvency' of a business is assessed by Financial Statement Analysis?

Ans. Solvency of a business is assessed through solvency ratios, *i.e.*, debt equity ratio, total assets to debt ratio and proprietary ratio.

Q. 13. How the 'Earning Capacity of a business' is assessed by Financial Statement Analysis?

Ans. Earning Capacity is assessed through 'Profitability' ratios.

Q. 14. How is 'window dressing' a limitation of Financial Statement Analysis?

Ans. Window dressing refers to the manipulation of accounts to conceal vital facts and presentation of the 'Financial Statements' in a way so as to show a position better than what it actually is. On account of such a situation financial analysis may give false information to the users.

Q. 15. Explain how Financial Statements Analysis ignores qualitative elements?

Ans. The qualitative elements like quality of management, quality of labour force, public relations etc. are ignored while carrying out the Analysis of Financial Statements.

Q. 16. Give any two differences between horizontal analysis and vertical analysis of financial statements. *(I.S.C. 2018)*

Multiple Choice Questions

Choose the Best Alternate :

Q. 1. Feature of financial analysis is to present the data contained in financial statements in

(A) Easy form
(B) Convenient and rational groups
(C) Comparable form
(D) All of the Above

Q. 2. Which analysis is considered as dynamic :

(A) Horizontal Analysis
(B) Vertical Analysis
(C) Internal Analysis
(D) External Analysis

Q. 3. Which analysis is considered as static :

(A) Horizontal Analysis
(B) Vertical Analysis
(C) Internal Analysis
(D) External Analysis

Q. 4. Which analysis is based only on one year's data :

(A) Cash Flow Statement
(B) Dividend Analysis
(C) Vertical Analysis
(D) Horizontal Analysis

Q. 5. Main objective of analysis of financial statements is

(A) To know the financial strength
(B) To make a comparative study with other firms
(C) To know the efficiency of management
(D) All of the Above

Q. 6. Analysis of Financial Statements is significant :

(A) For Creditors
(B) For Managers
(C) For Employees
(D) For all of the above

Q. 7. Financial analysis becomes significant because it :

(A) Ignores price level changes
(B) Measures the efficiency of business
(C) Lacks qualitative analysis
(D) Is effected by personal bias

Q. 8. When bad position of the business is tried to be depicted as good, it is known as ....

(A) Personal Bias
(B) Price Level Changes
(C) Window Dressing
(D) All of the Above

Q. 9. For whom the analysis of financial statements is not significant?

(A) Investor
(B) Government
(C) Ambassador of India
(D) Company's Employee

Q. 10. Main limitation of analysis of financial statements is

(A) Affected by window dressing
(B) Difficulty in forecasting
(C) Do not reflect changes in price level
(D) All of the Above

Q. 11. Which of the following is a limitation of financial analysis?

(A) It is just a study of reports of the company.
(B) It judges the ability of the firm to repay its debts.
(C) It identifies the reasons for change in financial position.
(D) It ascertains the relative importance of different components of the financial position of the firm. *(C.B.S.E. 2020; Kerala)*

Q. 12. Which of the following is not a limitation of analysis of financial statements?

(A) Affected by personal bias

(B) Inter firm comparative study possible
(C) Lack of Qualitative Analysis
(D) Ignores price level changes *(C.B.S.E. 2020; Lucknow, Kolkata)*

Q. 13. Which of the following is **not** an objective of Analysis of Financial Statements:
(A) To judge the financial health of the firm.
(B) To judge the short-term and long-term liquidity position of the firm.
(C) To judge the reasons for change in the profitability of the firm.
(D) To judge the variations in the accounting practices of the business followed by different enterprises. *(C.B.S.E. 2020; Mumbai, Chennai)*

Q. 14. Financial analysis become useless because it :
(A) Measures the profitability
(B) Measures the Solvency
(C) Lacks Qualitative Analysis
(D) Makes a comparative study

Q. 15. Parties interested in financial analysis are :
(A) Investors
(B) Government
(C) Financial Institutions
(D) All of the Above

Q. 16. Main limitation of financial analysis is :
(A) To know earning capacity
(B) To know financial strength
(C) Do not reflect changes in price level
(D) Comparative study with other firms

Q. 17. For whom analysis of financial statements is **not** significant?
(A) Political Adviser of Prime Minister
(B) Investors
(C) Management
(D) Financial Institutions

Q. 18. Which of the following is **not** a limitation of analysis of financial statements?
(A) Window Dressing
(B) Price level changes ignored
(C) Subjectivity
(D) Intra firm comparison possible
(C.B.S.E. 2020; Punjab)

Q. 19. Which of the following statements are **false**?

(*i*) When all the comparative figures in a balance sheet are stated as percentage of the total, it is termed as horizontal analysis.

(*ii*) When financial statements of several years are analysed, it is termed as vertical analysis.

(*iii*) Vertical analysis is also termed as time series analysis.

Choose from the following options :

(A) Both (*i*) and (*ii*)
(B) Both (*i*) and (*iii*)
(C) Both (*ii*) and (*iii*)
(D) All three (*i*), (*ii*), (*iii*)
(C.B.S.E. Sample Paper, 2021)

Q. 20. Which of the following are the tools of Vertical Analysis?

(*i*) Ratio Analysis.
(*ii*) Comparative Statements.
(*iii*) Common Size Statements.

(A) Only (*iii*)
(B) Both (*i*) and (*iii*)
(C) Both (*i*) and (*ii*)
(D) Only (*i*)

(C.B.S.E. Sample Paper, 2021)

(See Answers at the end of the book.)

11

Tools for Financial Analysis : Comparative Statements

Tools for Financial Analysis :

Financial statements contain absolute figures of assets, liabilities, revenues, expenses and profit or loss of an enterprise. They do not reveal the earning capacity, liquidity and financial soundness of the enterprise. They are not readily understandable to their users. Hence, they are analysed to present them in simple and understandable form. Various tools or devices employed for analysing the financial statements are as follows :

(1) Comparative Statements
(2) Common Size Statements
(3) Trend Analysis
(4) Accounting Ratios
(5) Cash Flow Statement
(6) Funds Flow Statement
(7) Break-Even Point Analysis

(1) **Comparative Statements :** When financial statements figures for two or more years are placed side-by-side to facilitate comparison, these are called 'Comparative Financial Statements'. In such a statement figures of production, revenue from operations*, expenses, profits etc. are put side-by-side to draw conclusions about the profitability and financial health of the business. It also indicates the trend of change as well as the strong points and weak points of the enterprise. Comparative statements have been discussed in this chapter.

(2) **Common Size Statements :** In these statements, various figures are converted into percentages to some common base. In profit and loss statement, revenue from operations figure is taken at 100 and all other figures are expressed as percentage of revenue from operations. Similarly, in balance sheet total assets are taken at 100 and all assets are expressed as percentage of the total. These statements have been discussed in Chapter 11.

(3) **Trend Analysis :** It is one of the most useful form of horizontal analysis in making comparative study of the financial statements for a number of years. For calculating trend percentages any year is selected as the 'base year'. Each item of the base year is assumed to be equal to 100 and on that basis the percentage of each item of each year is calculated. The trend percentage is helpful in revealing the trend — increase or decrease in various items. Trend percentages have been discussed in Chapter 11.

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* Schedule III has used the words 'Revenue from Operations' in place of Sales.

(4) **Accounting Ratios :** A ratio is simply one number expressed in relation to another and a study of the relationships between various items or groups of items is known as 'ratio analysis'. It simplifies and summarises a long array of accounting data to provide useful information regarding the liquidity, solvency, profitability etc. Accounting ratios have been discussed in Chapter 13.

(5) **Cash Flow Statement :** It shows the inflows and outflows of cash and cash equivalents during a particular period and analyses the reasons for changes in balance of cash between the two balance sheet dates. A firm may earn huge profits yet it may have paucity of cash or when it suffered a loss it may still have plenty of cash. The reasons for these deviations can be analysed and understood by preparing cash flow statement. It has been discussed in Chapter 12.

(6) **Funds Flow Statement :** A fund flow statement is designed to show the changes in the assets, liabilities and capital of the firm between the dates of two balance sheets. It indicates the causes of changes in the working capital of an enterprise during the year. It also discloses the sources from which funds were obtained by the enterprise and the specific uses to which such funds were applied.

(7) **Break-Even Point Analysis :** Break-Even Point is the point where total costs are exactly equal to the total sales. At this point, there is neither any profit nor any loss. It can also be termed as 'No-profit–No-loss' point.

It is not necessary that all the above-mentioned tools of financial analysis are used at one stretch. Selection of an appropriate tool depends on the object and the circumstances of the analysis. It is quite possible that the tool of analysis suitable to one investigator may be unsuitable to another investigator. As such, the tool of analysis should be selected very carefully.

COMPARATIVE STATEMENTS

In order to estimate the future progress of a firm, it is necessary to look into its past performance. For this purpose, it becomes essential to make comparative study of its financial statements for two or more years.

When financial statements figures for two or more years are placed side-by-side to facilitate comparison, these are called 'Comparative Financial Statements.' Such statements not only show the absolute figures of various years but also provide for columns to indicate the increase or decrease in these figures from one year to another. In addition, these statements may also show the change from one year to another in percentage form. Such comparative statements are of great value in forming the opinion regarding the progress of the enterprise.

When financial statements of two or more years of the same firm are presented and compared, it is known as inter-period comparison or intra-firm comparison. When financial statements of two or more firms are compared over a number of years, this is known as inter-firm comparison.

Purpose or Utility or Importance of Comparative Statements

(1) **To make the data simpler and more understandable :** The main aim of preparing comparative financial statements is to put the data for a number of years in simpler and comparable form. When data for a number of years are put side-by-side, a

comparison becomes easier and it becomes simpler to draw conclusions about the operating results and financial health of the concern.

(2) **To Indicate the Trend :** Comparative financial statements indicate the trend of change by putting the figures of production, revenue from operations, expenses and profits etc. for a number of years side-by-side. For example, if revenue from operations are increasing over the years along with increase in profit margins, it is an indication of healthy trend of the growth of the business.

(3) **To indicate the Strong Points and Weak Points of the Concern :** Comparison of financial statements for a number of years may also indicate the strong points and weak points of the firm. Management can then investigate and find out the reasons for the weaknesses of the concern and can take corrective measures.

(4) **To Compare the Firm's Performance with the Average Performance of the Industry :** Comparative financial statements help a business unit to compare its performance with the average performance of the industry (*i.e.*, all the firms in the same business).

(5) **To Help in Forecasting :** Comparative study of the changes in the key figures over a period helps the management in forecasting the profitability and financial soundness of the business.

The American Institute of Certified Public Accountants has explained the utility of preparing the Comparative Financial Statements as follows :

"The presentation of Comparative Financial Statements in annual and other reports enhances the usefulness of such reports and brings out more clearly the nature and trends of current changes affecting the enterprise. Such presentation emphasises the fact that statements for a series of periods are far more significant than those for a single period and that the accounts for one period are but an instalment of what is essentially a continuous history."

Because of the utmost usefulness of the comparative statements, the Companies Act, 2013 has provided that the Statement of Profit & Loss and Balance Sheet of a Company (Under Schedule III) must show the figures of the previous year also along with the figures of the current year.

However, for a valid comparison of financial statements, it is necessary that the statements should be prepared according to the generally accepted accounting principles and there should be no change in the accounting policies of a firm over the period of comparison, *i.e.*, the method of charging depreciation, valuation of inventory etc. should remain the same, otherwise the comparison will loose its significance and will become misleading.

Forms (Techniques) of Presenting Comparative Statements

Comparative statements may be presented in any of the following forms :

(1) **To Show the Absolute Data in Rupee Amount Only :** Sometimes only rupee amounts for various periods are shown in the comparative financial statements. For example, revenue from operations in 2019 is ₹2,00,000 and in 2020 is ₹2,50,000.

(2) **To Show the Increases and Decreases in Absolute Data in Terms of Money Values :** For example, in comparison to 2019 revenue from operations in 2020 increased by ₹50,000.

(3) **To Show the Increases and Decreases in Absolute Data in Terms of Percentages :** For example, in comparison to 2019 revenue from operations in 2020 increased by 25%.

(4) **Comparisons Expressed in Ratios :** Sometimes an additional column is provided in the comparative financial statements to show the changes over the years in terms of ratio. Data of current year is divided by the data of previous year. Ratio of more than 1 will indicate an increase while a ratio of less than 1 will indicate a decrease in the current year in comparison to previous year. For example, if the revenue from operations in 2019 are ₹2,00,000 and revenue from operations in 2020 are ₹2,50,000, the ratio will be $\frac{2,50,000}{2,00,000} = 1.25$.

(5) **Use of Cumulative Figures and Averages .—** For example, revenue from operations in 2017, 2018, 2019 and 2020 were ₹2,10,000; ₹1,80,000; ₹2,00,000 and ₹2,50,000 respectively.

$$\text{Average revenue from operations} = \frac{8,40,000}{4} = ₹2,10,000.$$

This average figure of revenue from operations is used for comparing the individual figure of revenue from operations of each year and deviations are calculated.

Various types of financial statements are prepared in comparative form for the purpose of analysis but in practice, generally the statement of Profit & Loss and balance sheet are alone prepared in a comparative form because they are the most important financial statements. The two have been discussed below :

Comparative Balance Sheet

The Comparative Balance Sheet shows increases and decreases in the various assets, liabilities and in capital.

Advantages of Comparative Balance Sheet :

(1) A single year's balance sheet shows only the balances of accounts on a particular date, whereas the comparative balance sheet shows not only the balances of accounts as on different dates but also the extent of increase or decrease in various items of balance sheet.

(2) In a single year's balance sheet the focus is on status, whereas in a Comparative balance sheet emphasis is on change.

(3) A comparative balance sheet is more useful in comparison to a single year's balance sheet, because it enables a financial analyst to study the nature, size and direction of change, *i.e.*, increase or decrease in various items of balance sheet. As such, it may be used to study the trends in business concern.

(4) The Comparative Balance Sheet is a connecting link between the Statement of Profit & Loss and the Balance Sheet, because the statement of profit & loss presents the result of operating activities of a business, whereas the Comparative balance sheet shows the effect of operating activities on its assets, liabilities and capital.

Format of Comparative Balance Sheet :

The format of comparative balance sheet consists of five columns. In the first column the items of Balance Sheet are entered. In the second column the data for current year is shown and in the third column the data for previous year is shown. In the fourth column the increases or decreases in absolute data is shown in terms of rupee amounts. Fifth column shows the percentage of increase or decrease in absolute data.

Format of a Comparative Balance Sheet :

Format of a Comparative Balance Sheet in accordance with the Vertical form of presentation as per Schedule III is as under :

COMPARATIVE BALANCE SHEET
*as at 31st March 2022 and 2021**

Particulars	*Note No.*	*2022*	*2021*	*Absolute Change Increase/ Decrease*	*Percentage Increase/ Decrease*
1		2	3	4	5
I. EQUITY AND LIABILITIES :		₹	₹	₹	%
1. Shareholder's Funds					
(*a*) Share Capital		...	...	...	...
(*b*) Reserve and Surplus		...	...	...	...
2. Non Current Liabilities :					
(*a*) Long term Borrowings		...	...	...	...
(*b*) Long term Provisions		...	...	...	...
3. Current Liabilities :					
(*a*) Short term Borrowings		...	...	...	...
(*b*) Trade Payables		...	...	...	...
(*c*) Other Current Liabilities		...	...	...	...
(*d*) Short term Provisions		...	...	...	...
TOTAL		...	...	...	...
II. ASSETS :					
1. Non Current Assets :					
(*a*) Fixed Assets :					
(*i*) Tangible Assets		...	...	...	...
(*ii*) Intangible Assets		...	...	...	...
(*b*) Non-Current Investments		...	...	...	...
(*c*) Long term Loans and Advances		...	...	...	...
2. Current Assets :					
(*a*) Current Investments		...	...	...	...
(*b*) Inventories		...	...	...	...
(*c*) Trade Receivables		...	...	...	...
(*d*) Cash and Bank Balance		...	...	...	...

(*e*) Short-term Loans and Advances		...	...	...	...
(*f*) Other Current Assets		...	...	...	...
TOTAL		...	...	...	...

*As per the new format of Balance Sheet given in Schedule III, Balance Sheet of current year should be presented first and of previous year thereafter.

The preparation of comparative balance sheet has been explained in the following illustrations :

ILLUSTRATION 1

From the following Balance Sheets of Usha Chemicals Ltd. as at 31st March, 2022 and 2021, prepare a Comparative Balance Sheet :

Particulars	*Note No.*	*31.3.2022**	*31.3.2021*
		₹	₹
I. EQUITY AND LIABILITIES :			
1. Shareholder's Funds :			
(*a*) Share Capital		10,00,000	5,00,000
(*b*) Reserves and Surplus		2,00,000	3,00,000
2. Non-Current Liabilities			
Long term Borrowings		8,00,000	5,00,000
3. Current Liabilities			
Trade Payables		4,00,000	2,00,000
TOTAL		24,00,000	15,00,000
II. ASSETS :			
1. Non Current Assets			
Fixed Assets :			
(*i*) Tangible Assets		14,00,000	8,00,000
(*ii*) Intangible Assets		3,00,000	2,00,000
2. Current Assets			
(*a*) Inventories		5,00,000	4,00,000
(*b*) Cash and Bank Balance		2,00,000	1,00,000
TOTAL		24,00,000	15,00,000

*As per Revised Format, Balance Sheet of current year will be given first.

SOLUTION :

COMPARATIVE BALANCE SHEET OF USHA CHEMICALS LTD.

as at 31st March, 2022 and 2021

Particulars	*Note No.*	*2022*	*2021*	*Absolute Change Increase/ Decrease*	*Percentage Increase/ Decrease*
1		2	3	4	5
		₹	₹	₹	%
I. EQUITY AND LIABILITIES :					

1. **Shareholder's Funds**					
(*a*) Share Capital		10,00,000	5,00,000	5,00,000	100.00$^{(1)}$
(*b*) Reserve and Surplus		2,00,000	3,00,000	(1,00,000)*	(33.33)$^{(2)}$
2. **Non Current Liabilities :**					
Long term Borrowings		8,00,000	5,00,000	3,00,000	60.00
3. **Current Liabilities :**					
Trade Payables		4,00,000	2,00,000	2,00,000	100.00
TOTAL		24,00,000	15,00,000	9,00,000	60.00
II. ASSETS					
1. **Non Current Assets :**					
Fixed Assets					
(*i*) Tangible Assets		14,00,000	8,00,000	6,00,000	75.00
(*ii*) Intangible Assets		3,00,000	2,00,000	1,00,000	50.00
2. **Current Assets :**					
(*a*) Inventories		5,00,000	4,00,000	1,00,000	25.00
(*b*) Cash and Bank Balance		2,00,000	1,00,000	1,00,000	100.00
TOTAL		24,00,000	15,00,000	9,00,000	60.00

* Bracket denotes negative item.

Working Notes : Calculation of percentage Increase or Decrease is as follows :

$$\frac{\text{Increase or Decrease over 2021}}{\text{Absolute Figure of 2021}} \times 100$$

(1) $\frac{5,00,000}{5,00,000} \times 100 = 100\%$ Increase

(2) $\frac{1,00,000}{3,00,000} \times 100 = 33.33\%$ decrease and so on.

ILLUSTRATION 2.

From the following information, prepare Comparative Balance Sheets of *X* Ltd. :

Particulars	*31.3.2022*	*31.3.2021*
	₹	₹
Reserve and Surplus	12,00,000	6,00,000
Share Capital	10,00,000	10,00,000
Trade Payables	12,70,000	9,00,000
Land and Buildings	16,00,000	15,00,000
Plant and Machinery	6,30,000	5,00,000
Goodwill	—	1,00,000
Investments	1,20,000	1,00,000
Current Assets	15,20,000	8,00,000
Long term Borrowings	4,00,000	5,00,000

SOLUTION : COMPARATIVE BALANCE SHEET OF *X* LTD.

as at 31st March 2022 and 2021

Particulars	Note No.	2022*	2021	Absolute Change Increase/ Decrease	Percentage Increase/ Decrease
1		2	3	4	5
		₹	₹	₹	%
I. EQUITY AND LIABILITIES					
1. Shareholder's Funds :					
(*a*) Share Capital		10,00,000	10,00,000	—	—
(*b*) Reserves and Surplus		12,00,000	6,00,000	6,00,000	100.00
2. Non Current Liabilities					
Long term Borrowings		4,00,000	5,00,000	(1,00,000)	(20.00)*
3. Current Liabilities					
Trade Payables		12,70,000	9,00,000	3,70,000	41.11
TOTAL		38,70,000	30,00,000	8,70,000	29.00
II. ASSETS					
1. Non Current Assets					
(*a*) Fixed Assets					
(*i*) Tangible Assets	1	22,30,000	20,00,000	2,30,000	11.50
(*ii*) Intangible Assets	2	—	1,00,000	(1,00,000)	(100.00)
(*b*) Investments		1,20,000	1,00,000	20,000	20.00
2. Current Assets		15,20,000	8,00,000	7,20,000	90.00
TOTAL		38,70,000	30,00,000	8,70,000	29.00

*As per Revised Format Balance Sheet of Current Year *i.e.*, 31-3-2022 should be presented first.

Note :

	31.3.2022	31.3.2021
(1) Tangible Assets :		
Land and Buildings	16,00,000	15,00,000
Plant and Machinery	6,30,000	5,00,000
	22,30,000	20,00,000
(2) Intangible Assets :		
Goodwill	—	1,00,000

* Bracket denotes negative balance.

ILLUSTRATION 3.

From the following Balance Sheets of M/s Ram Nath & Co., prepare a Comparative Balance Sheet and comment upon the changes :

BALANCE SHEETS

as at 31st March..............

(Figures in thousand ₹)

Particulars	Note No.	31.3.2022	31.3.2021
I. EQUITY AND LIABILITIES :		₹	₹
1. Shareholder's Funds :			

(*a*) Share Capital		3,300	2,800
(*b*) Reserves and Surplus		1,400	1,000
2. Non-Current Liabilities :			
Long-term Borrowings		510	600
3. Current Liabilities :			
(*a*) Short term Borrowings		860	600
(*b*) Trade Payables		430	250
		6,500	5,250
II. ASSETS :			
1. Non-Current Assets		3,630	2,130
2. Current Asets			
(*a*) Inventory		1,100	1,500
(*b*) Trade Receivables		1,400	1,280
(*c*) Cash and Bank Balance		370	340
		6,500	5,250

SOLUTION :

COMPARATIVE BALANCE SHEET

as at 31st March, 2022 and 2021

(Figures in thousand ₹)

Particulars	*Note No.*	*2022*	*2021*	*Absolute Change Increase/ Decrease*	*Percentage Increase/ Decrease*
1		2	3	4	5
		₹	₹	₹	%
I. EQUITY AND LIABILITIES					
1. Shareholder's Funds					
(*a*) Share Capital		3,300	2,800	500	17.86
(*b*) Reserves and Surplus		1,400	1,000	400	40.00
2. Non Current Liabilities :					
Long term Borrowings		510	600	(90)	(15.00)
3. Current Liabilities					
(*a*) Short term Borrowings		860	600	260	43.33
(*b*) Trade Payables		430	250	180	72.00
TOTAL		6,500	5,250	1,250	23.81
II. ASSETS					
1. Non Current Assets		3,630	2,130	1,500	70.42
2. Current Assets :					
(*a*) Inventory		1,100	1,500	(400)	(26.67)
(*b*) Trade Receivables		1,400	1,280	120	9.38
(*c*) Cash and Bank Balance		370	340	30	8.82
TOTAL		6,500	5,250	1,250	23.81

Comments : The analysis of the above comparative balance sheets gives the following conclusions :

(1) Non-Current Assets have increased by ₹15,00,000, *i.e.*, 70.42% increase.

(2) Purchase of Non-Current Assets was financed partly by the issue of new equity shares for ₹5,00,000 and partly by the increase of ₹4,00,000 in reserves and partly by decrease of ₹2,50,000 in current assets and the balance have been arranged by delaying the payment of current liabilities.

(3) Equity share capital has increased by ₹5,00,000, *i.e.*, 17.86% increase. It has made the financial position of the company strong.

(4) Reserves have increased by ₹4,00,000, *i.e.*, 40% increase, which reflects the increase in profits. It has also made the financial position of the company strong.

Comparative Statement of Profit and Loss

Profit and Loss Statement shows the net profit or net loss of that year. A comparative statement of profit and loss shows the net profits for a number of years so that changes in absolute data in terms of money as well as in terms of percentages may be known. Comparative statement of profit and loss provides the following informations:

I. Rate of increase or decrease in revenue from operations.

II. Rate of increase or decrease in cost of materials consumed.

III. Rate of increase or decrease in incomes and expenses.

IV. Rate of increase or decrease in net profit.

Objectives of Comparative Statement of Profit & Loss :

(*i*) To facilitate comparison of various items of income and expenditure for two or more years.

(*ii*) To analyse the increase or decrease in the income and expenditure in terms of rupee and also in percentage from one year to another.

(*iii*) To analyse the increase or decrease in the profits of the enterprise.

(*iv*) To help in forecasting the profitability of the business concern.

Format of Comparative Statement of Profit & Loss :

The format of comparative statement of profit and loss also consists of five columns. In the first column items of Statement of Profit & Loss are shown. In the second column the data for current year is shown and in the third column the data for previous year is shown. In the fourth column the increase or decrease in absolute data is shown in terms of rupee amounts. Fifth column shows the increase or decrease in various items in the form of percentages.

Format of a Comparative Statement of Profit & Loss

COMPARATIVE STATEMENT OF PROFIT & LOSS
for the years ended 31st March 2022 and 2021

Particulars	*Note No.*	*2021-22*	*2020-21*	*Absolute Change (Increase/ Decrease)*	*Percentage (Increase/ Decrease)*
1		2	3	4	5
		A	B	(A – B) = C	$\frac{C}{B}\times 100$ = D
		₹	₹	₹	%
I. Revenue from Operations		. . .	. . .	. . .	. . .
II. *Add* : Other Incomes		. . .	. . .	. . .	. . .
III. Total Revenue I + II		. . .	. . .	. . .	. . .
IV. *Less* : Expenses					
Cost of Materials Consumed		. . .	. . .	. . .	. . .
Purchase of Stock in Trade		. . .	. . .	. . .	. . .
Changes in Inventories of Finished Goods, Work-in-Progress and Stock in Trade		. . .	. . .	. . .	. . .
Employee Benefit Expenses		. . .	. . .	. . .	. . .
Finance Costs		. . .	. . .	. . .	. . .
Depreciation and Amortization Exp.		. . .	. . .	. . .	. . .
Other Expenses		. . .	. . .	. . .	. . .
Total Expenses		. . .	. . .	. . .	. . .
V. Profit before Tax (III – IV)		. . .	. . .	. . .	. . .
VI. *Less* : Tax		(. . .)	(. . .)	(. . .)	(. . .)
VII. Profit after Tax (V – VI)		. . .	. . .	. . .	. . .

Important Note : Comments on Comparative/Common-Size financial statements are not a part of the scope of the syllabus.

Comparative statement of profit & loss has been explained in the following illustrations :

ILLUSTRATION 4.

From the following information, prepare a Comparative Statement of Profit & Loss :

Particulars	*Note No.*	*31.3.2022*	*31.3.2021*
		₹	₹
Revenue from Operations		75,00,000	60,00,000

Other Incomes		1,20,000	1,50,000
Expenses		50,60,000	44,00,000
Income Tax		40%	35%

SOLUTION : COMPARATIVE STATEMENT OF PROFIT & LOSS
for the years ended 31st March 2022 and 2021

Particulars	*Note No.*	*2021-22*	*2020-21*	*Absolute Change (Increase/ Decrease)*	*Percentage (Increase/ Decrease)*
1		2	3	4	5
		A	B	(A – B) = C	$\frac{C}{B} \times 100$ = D
		₹	₹	₹	%
I. Revenue from Operations		75,00,000	60,00,000	15,00,000	25.00
II. *Add* : Other Incomes		1,20,000	1,50,000	(30,000)*	(20.00)
III. Total Revenue I + II		76,20,000	61,50,000	14,70,000	23.90
IV. *Less* : Expenses		50,60,000	44,00,000	6,60,000	15.00
V. Profit before Tax (III – IV)		25,60,000	17,50,000	8,10,000	46.29
VI. *Less* : Tax		10,24,000	6,12,500	4,11,500	67.18
VII. Profit after Tax (V – VI)		15,36,000	11,37,500	3,98,500	35.03

* Bracket denotes negative items.

ILLUSTRATION 5

From the following information, prepare a Comparative Statement of Profit & Loss :

Particulars	*Note No.*	*31.3.2022*	*31.3.2021*
		₹	₹
Revenue from Operations		5,00,000	4,00,000
Expenses		4,00,000	2,40,000
Other Incomes		30,000	20,000
Income Tax		70,000	60,000

SOLUTION : COMPARATIVE STATEMENT OF PROFIT & LOSS
for the years ended 31st March 2022 and 2021

Particulars	*Note No.*	*2021-22*	*2020-21*	*Absolute Change (Increase/ Decrease)*	*Percentage Increase/ Decrease*
1		2	3	4	5
		A	B	(A – B) = C	$\frac{C}{B} \times 100$ = D
		₹	₹	₹	%

I. Revenue from Operations		5,00,000	4,00,000	1,00,000	25.00
II. *Add* : Other Incomes		30,000	20,000	10,000	50.00
III. Total Revenue I + II		5,30,000	4,20,000	1,10,000	26.19
IV. *Less* : Expenses		4,00,000	2,40,000	1,60,000	66.67
V. Profit before Tax (III – IV)		1,30,000	1,80,000	(50,000)	(27.78)
VI. *Less* : Tax		70,000	60,000	10,000	16.67
VII. Profit after Tax (V – VI)		60,000	1,20,000	(60,000)	(50.00)

ILLUSTRATION 6.

Prepare a Comparative Statement of Profit & Loss from the following :

	Note No.	*31st March, 2021*	*31st March, 2022*
		₹	₹
Revenue from Operations		10,00,000	12,50,000
Cost of Materials Consumed		5,00,000	6,50,000
Other Expenses		50,000	60,000

Interest on investments @ ₹30,000 each year.

SOLUTION :

COMPARATIVE STATEMENT OF PROFIT & LOSS

for the years ended 31st March 2022 and 2021

Particulars	*Note No.*	*2021-22*	*2020-21*	*Absolute Change (Increase/ Decrease)*	*Percentage Increase/ Decrease*
1		2	3	4	5
		A	B	(A – B) = C	$\frac{C}{B} \times 100$ = D
		₹	₹	₹	%
I. Revenue from Operations		12,50,000	10,00,000	2,50,000	25.00
II. *Add* : Other Incomes		30,000	30,000	—	—
III. Total Revenue I + II		12,80,000	10,30,000	2,50,000	24.27
IV. *Less* : Expenses					
Cost of Materials Consumed		6,50,000	5,00,000	1,50,000	30.00
Other Expenses		60,000	50,000	10,000	20.00
Total Expenses		7,10,000	5,50,000	1,60,000	29.09
V. Profit before Tax (III – IV)		5,70,000	4,80,000	90,000	18.75

Note : As per new format under Schedule III figures of current year *i.e.*, 2022 should be presented first and figures of previous year *i.e.*, 2021 thereafter.

ILLUSTRATION 7.

Prepare a comparative statement of profit & loss of *X* Ltd., with the help of the following information :

	Note No.	31.3.2020	31.3.2019
Revenue from Operations		₹20,00,000	₹10,00,000
Cost of Materials Consumed		70% of Revenue from Operations	60% of Revenue from Operations
Other Expenses		60,000	40,000
Rate of Income Tax		50% of Net Profit before Tax	

SOLUTION :

COMPARATIVE STATEMENT OF PROFIT & LOSS
for the years ended 31st March 2020 and 2019

Particulars	*Note No.*	*2019-20*	*2018-19*	*Absolute Change (Increase/ Decrease)*	*Percentage (Increase/ Decrease)*
1		*2*	*3*	*4*	*5*
		A	*B*	*(A – B) = C*	$\frac{C}{B} \times 100 = D$
		₹	₹	₹	%
I. Revenue from Operations		20,00,000	10,00,000	10,00,000	100.00
II. *Less* : Expenses :					
Cost of Materials Consumed		14,00,000	6,00,000	8,00,000	133.33
Other Expenses		60,000	40,000	20,000	50.00
Total Expenses		14,60,000	6,40,000	8,20,000	128.13
III. Profit before Tax (I – II)		5,40,000	3,60,000	1,80,000	50.00
IV. *Less* : Tax		2,70,000	1,80,000	90,000	50.00
V. Profit after Tax (III – IV)		2,70,000	1,80,000	90,000	50.00

ILLUSTRATION 8.

From the following information prepare a Comparative Statement of Profit & Loss of Victor Ltd. :

	Note No.	31.3.2020	31.3.2019
		₹	₹
Revenue from Operations		18,00,000	15,00,000
Cost of Materials Consumed		14,00,000	11,00,000
Other Expenses		12% of Materials Consumed	10% of Materials Consumed
Income Tax		50%	40%

SOLUTION : COMPARATIVE STATEMENT OF PROFIT & LOSS

for the years ended 31st March 2020 and 2019

Particulars	*Note No.*	*2019-20*	*2018-19*	*Absolute Change (Increase/ Decrease)*	*Percentage (Increase/ Decrease)*
1		*2*	*3*	*4*	*5*
		A	*B*	*(A – B) = C*	$\frac{C}{B} \times 100$ = D
		₹	₹	₹	%
I. Revenue from Operations		18,00,000	15,00,000	3,00,000	20.00
II. *Less* : Expenses					
Cost of Materials Consumed		14,00,000	11,00,000	3,00,000	27.27
Other Expenses		1,68,000	1,10,000	58,000	52.73
Total Expenses		15,68,000	12,10,000	3,58,000	29.59
III. Profit before Tax (I – II)		2,32,000	2,90,000	(58,000)	(20.00)
IV. *Less* : Tax		1,16,000	1,16,000	—	—
V. Profit after Tax (III – IV)		1,16,000	1,74,000	(58,000)	(33.33)

ILLUSTRATION 9

Prepare a Comparative Statement of Profit & Loss of Ahmed Ltd., with the help of the following information :

	Note No.	*31.3.2020*	*31.3.2019*
		₹	₹
Revenue from Operations		8,00,000	5,00,000
Purchase of Stock in Trade		4,20,000	2,40,000
Changes in Inventories		80,000	60,000
Employee Benefit Expenses*		20,000	40,000
Other Expenses		40,000	30,000
Income Tax		50%	40%

* Employee Benefit Expenses means expenses incurred on employees. It includes expenses such as salaries and wages, contribution to Provident Fund, staff welfare etc.

SOLUTION : COMPARATIVE STATEMENT OF PROFIT & LOSS

for the years ended 31st March 2020 and 2019

Particulars	*Note No.*	*2019-20*	*2018-19*	*Absolute Change Increase/ Decrease*	*Percentage Increase/ Decrease)*
1		*2*	*3*	*4*	*5*
		A	*B*	*(A – B) = C*	$\frac{C}{B} \times 100$ = D
		₹	₹	₹	%

I. Revenue from Operations		8,00,000	5,00,000	3,00,000	60.00
II. *Less* : Expenses					
Purchase of Stock in Trade		4,20,000	2,40,000	1,80,000	75.00
Change in Inventories*		80,000	60,000	20,000	33.33
Employee Benefit Expenses		20,000	40,000	(20,000)	(50.00)
Other Expenses		40,000	30,000	10,000	33.33
Total Expenses		5,60,000	3,70,000	1,90,000	51.35
III. Profit before Tax (I – II)		2,40,000	1,30,000	1,10,000	84.62
IV. *Less* : Tax		1,20,000	52,000	68,000	130.77
V. Profit after Tax (III – IV)		1,20,000	78,000	42,000	53.85

* Changes in Inventories means Opening Stock *less* Closing Stock.

ILLUSTRATION 12

Prepare a Comparative Statement of Profit & Loss from the following information:

Particulars	*Note No.*	*31-3-2019*	*31-3-2020*
		₹	₹
Revenue from Operations		30,00,000	40,00,000
Purchase of Stock in Trade		19,00,000	20,00,000
Changes in Inventories		(1,00,000)	2,00,000
Other Expenses		1,80,000	1,76,000

SOLUTION : COMPARATIVE STATEMENT OF PROFIT & LOSS

for the years ended 31st March 2020 and 2019

Particulars	*Note No.*	*2019-20*	*2018-19*	*Absolute Change (Increase/ Decrease)*	*Percentage (Increase/ Decrease)*
1		*2*	*3*	*4*	*5*
		A	*B*	*(A – B) = C*	$\frac{C}{B} \times 100$ = D
		₹	₹	₹	%
I. Revenue from Operations		40,00,000	30,00,000	10,00,000	33.33
II. *Less* : Expenses					
Purchases of Stock in Trade		20,00,000	19,00,000	1,00,000	5.26
Changes in Inventories		2,00,000	(1,00,000)	3,00,000	300.00
Other Expenses		1,76,000	1,80,000	(4,000)	(2.22)
Total Expenses		23,76,000	19,80,000	3,96,000	20.00
III. Profit before Tax (I – II)		16,24,000	10,20,000	6,04,000	59.22

Note : Figures of Current Year i.e., 2020 will be presented first.

ILLUSTRATION 11

From the following data, prepare statement of profits in comparative form :

Particulars	*Note No.*	*Year II*	*Year I*
		₹	₹
Revenue from Operations		8,00,000	6,00,000
Expenses		55% of Revenue from Operations	
Other Income		40,000	20,000
Income Tax Rate		40%	35%

SOLUTION : COMPARATIVE STATEMENT OF PROFIT & LOSS

for the years ended ....

Particulars	*Note No.*	*Year II*	*Year I*	*Absolute Change (Increase/ Decrease)*	*Percentage (Increase/ Decrease)*
1		*2*	*3*	*4*	*5*
		A	*B*	*(A – B) = C*	$\frac{C}{B} \times 100$ = D
		₹	₹	₹	%
I. Revenue from Operations		8,00,000	6,00,000	2,00,000	33.33
II. *Add* : Other Incomes		40,000	20,000	20,000	100.00
III. Total Revenue I + II		8,40,000	6,20,000	2,20,000	35.48
IV. *Less* : Expenses		4,40,000	3,30,000	1,10,000	33.33
V. Profit before Tax (III – IV)		4,00,000	2,90,000	1,10,000	37.93
VI. *Less* : Tax		1,60,000	1,01,500	58,500	57.64
VII. Profit after tax (V – VI)		2,40,000	1,88,500	51,500	27.32

ILLUSTRATION 12.

Prepare a Comparative Statement of Profit & Loss from the following :

Particulars	*31.3.2020*	*31.3.2019*
	₹	₹
Revenue from Operations	50,00,000	30,00,000
Finance Costs	30,00,000	27,00,000
Employee Benefit Expenses	4,00,000	3,00,000
Other Expenses	40,000	50,000
Income Tax 40% of Net Profit		

SOLUTION : COMPARATIVE STATEMENT OF PROFIT & LOSS

for the years ended 31st March 2020 and 2019

Particulars	*Note No.*	*2019-20*	*2018-19*	*Absolute Change (Increase/ Decrease)*	*Percentage (Increase/ Decrease)*
1		*2*	*3*	*4*	*5*
		A	*B*	*(A − B) = C*	$\frac{C}{B} \times 100$ = D
		₹	₹	₹	%
I. Revenue from Operations		50,00,000	30,00,000	20,00,000	66.67
II. *Less* : Expenses					
Employee Benefit Expenses		4,00,000	3,00,000	1,00,000	33.33
Finance Costs		30,00,000	27,00,000	3,00,000	11.11
Other Expenses		40,000	50,000	(10,000)	(20.00)
Total Expenses		34,40,000	30,50,000	3,90,000	12.79
III. Profit/Loss before Tax (I – II)		15,60,000	(50,000)	16,10,000	3220.00
IV. *Less* : Tax		6,24,000	—	6,24,000	—
V. Profit/Loss after Tax (III – IV)		9,36,000	(50,000)	9,86,000	1,972.00

ILLUSTRATION 13.

From the following information, prepare a Comparative Statement of Profit and Loss of Matrix Ltd. :

Particulars	*31.3.2016*	*31.3.2015*
	₹	₹
Revenue from Operations	3,00,000	2,50,000
Cost of Material consumed	1,70,000	1,50,000
Interest from Investments	20,000	20,000
Employee Benefit Expenses	10,000	10,000
Tax Rate	50%	50%

(I.S.C. 2017)

SOLUTION :

COMPARATIVE STATEMENT OF PROFIT & LOSS OF MATRIX LTD.

for the year ended 31-03-2016 and 31-03-2015

Particulars	*31-03-2016*	*31-03-2015*	*Absolute Change*	*Percentage Change*
	₹	₹	₹	%
I. Revenue from Operations	3,00,000	2,50,000	50,000	20
II. *Add* : Other Income	20,000	20,000	—	—
III. Total Revenue (I + II)	3,20,000	2,70,000	50,000	18.52

IV. *Less :* Expenses :				
Cost of Material consumed	1,70,000	1,50,000	20,000	13.33
Employee Benefit Expenses	10,000	10,000	—	—
Total Expenses	1,80,000	1,60,000	20,000	12.5
V. Profit Before Tax (III – IV)	1,40,000	1,10,000	30,000	27.27
Less : Tax	70,000	55,000	15,000	27.27
Profit After Tax	70,000	55,000	15,000	27.27

Short Answer Questions

(Questions Carrying 1 Mark)

Q. 1. Name two tools of financial analysis. *(ISC Sample Paper, 2017)*

Ans. (*i*) Comparative financial statements. (*ii*) Common Size financial statements.

Q. 2. What are comparative financial statements?

Ans. When financial statements figures for two or more years are placed side-by-side to facilitate comparison, these are called 'Comparative Financial Statements.' Such statements provide for columns to indicate the increase or decrease in these figures from one year to another in absolute figures and in percentage form.

Q. 3. Give two objectives of Comparative Financial Statements.

Ans. (1) **To make the data simpler and more understandable :** The main aim of preparing comparative financial statements is to put the data for a number of years in simpler and comparable form.

(2) **To indicate the trend :** Another aim of comparative financial statements is to indicate the trend of change by putting the figures of production, revenue from operations, expenses and profits etc. for a number of years side-by-side.

Q. 4. What is a Comparative Balance Sheet?

Ans. A Comparative Balance Sheet shows the increase and decrease in various assets liabilities and capital in two or more balance sheets of the same business enterprise on different dates.

Q. 5. Give two advantages of Comparative Balance Sheet.

(I.S.C. Specimen Question Paper, 2018)

Ans. (*i*) It shows the extent of increase or decrease in various items of balance sheet.

(*ii*) It throws light on nature, size and direction of change in respect of each item of balance sheet.

Q. 6. What is a Comparative Statement of Profit & Loss?

Ans. A Comparative Statement of Profit & Loss shows the figures of revenue from operations, expenses, incomes and net profit or loss for a number of years so that changes in absolute data in terms of money as well as in terms of percentages may be known.

Short Answer Questions

(Questions Carrying 2 Marks)

1. Give two objectives of Comparative Financial Statements.
2. Give two objectives of Comparative Balance Sheet.
3. What is Comparative Statement of Profit & Loss? How is it prepared?
4. Give a specimen of Comparative Balance Sheet of a Company for two years for comparison purpose.
5. Give a specimen of Comparative Statements of Profit & Loss for two years.
6. Take a few imaginary figures and prepare a Comparative Statement of Profit & Loss for two years.

PRACTICAL QUESTIONS

(Q. Nos. 1 to 12 are strictly in the serial order of Illustrations)

Q. 1. From the following Balance Sheets of Royal Industries as at 31st March, 2022 and 2021, prepare a comparative Balance Sheet :

Particulars	*Note No.*	*31.3.2022*	*31.3.2021*
I. EQUITY AND LIABILITIES :		₹	₹
1. Shareholder's Funds :			
(*a*) Share Capital		8,00,000	5,00,000
(*b*) Reserves and Surplus		1,00,000	1,00,000
2. Non-Current Liabilities			
Long term Borrowings		4,00,000	3,00,000
3. Current Liabilities			
Short term Borrowings		2,00,000	1,00,000
		15,00,000	10,00,000
II. ASSETS :			
1. Non-Current Assets		6,00,000	4,00,000
2. Current Assets :			
(*a*) Inventories		3,00,000	2,00,000
(*b*) Trade Receivables		4,00,000	3,00,000
(*c*) Cash and Bank Balance		2,00,000	1,00,000
		15,00,000	10,00,000

[Ans. Percentage Change in Share Capital 60.00; Reserves & Surplus Nil; Non Current Liabilities 33.33; Current Liabilities 100.00; Non Current Assets 50.00; Inventories 50.00; Trade Receivables 33.33; Cash and Bank Balance 100.00.]

Q. 2. From the following information, prepare Comparative Balance Sheet of *Y* Ltd. :

	31st March, 2022 (Figures being in Lakh of ₹)	31st March, 2021 (Figures being in Lakh of ₹)
Share Capital	25	20
Investments	9	5
Long-term Borrowings	12	9
Inventories	18	20
Cash and Bank Balance	2	5
Current Liabilities	12	15
Reserves	40	36
Tangible Assets	50	40
Intangible Assets	10	10

[Ans. Percentage change in Share Capital 25.00; Reserve and Surplus 11.11; Non Current Liabilities 33.33; Current Liabilities (20.00); Tangible Assets 25.00; Intangible Assets Nil; Investments 80.00; Inventories (10.00); Cash and Bank Balance (60.00).]

Q. 1. Prepare a Comparative Balance Sheet from the following and interpret it :

BALANCE SHEETS

as at 31st March ....

(Figures in thousand ₹)

Particulars	*Note No.*	*31.3.2022*	*31.3.2021*
I. EQUITY AND LIABILITIES :		₹	₹
1. Shareholder's Funds :			
(*a*) Share Capital		375	400
(*b*) Reserve & Surplus		72	60
2. Non-Current Liabilities			
Long term Borrowings		150	90
3. Current Liabilities			
Short term Borrowings		133	140
		730	690
II. ASSETS :			
1. Non-Current Assets		600	400
2. Current Assets :			
(*a*) Inventory		100	200
(*b*) Cash and Bank Balance		30	90
		730	690

[Ans. Percentage change in Share Capital (6.25); Reserve & Surplus 20.00; Non Current Liabilities 66.67; Current Liabilities (5.00); Non Current Assets 50.00; Inventory (50.00); Cash and Bank Balance (66.67)]

Q. 4. Prepare a comparative statement of Profit & Loss from the following data :

	Note No.	31.3.2022 ₹	31.3.2021 ₹
Revenue from Operations		18,00,000	15,00,000
Other Income		60,000	30,000
Expenses		10,40,000	8,70,000
Income Tax		3,00,000	2,50,000

[Ans. Profit After Tax : 2022 ₹5,20,000; 2021 ₹4,10,000.]

Percentage (%) Change in :

Revenue from Operations	Other Income	Total Revenue	Expenses	Profit before Tax	Profit After Tax
20.00	100.00	21.57	19.54	24.24	26.83

Q. 5. From the following details, make out a Comparative Statement of Profit & Loss :

	Note No.	31.3.2022 ₹	31.3.2021 ₹
Revenue from Operations		15,00,000	12,00,000
Expenses		8,05,000	7,00,000
Other Incomes		40,000	20,000
Provision for Tax		2,80,000	2,00,000

[Ans. Profit After Tax 2022 ₹4,55,000; 2021 ₹3,20,000.]

Percentage (%) Change in :

Revenue from Operations	Other Income	Total Revenue	Expenses	Profit before Tax	Profit After Tax
25.00	100.00	26.23	15.00	41.35	42.19

Q. 6. Prepare a Comparative Statement of Profit & Loss from the following :

Particulars	Note No.	31st March, 2022 ₹	31st March, 2021 ₹
Revenue from Operations		12,50,000	10,00,000
Cost of Materials Consumed		7,20,000	6,00,000
Other Expenses		38,000	40,000

Interest on investments @ ₹50,000 each year.

[Ans. Profit before Tax 2022 ₹5,42,000; 2021 ₹4,10,000.]

Percentage (%) Change in :

Revenue from Operations	Other Income	Total Revenue	Cost of Materials Consumed	Other Expenses	Profit before Tax
25.00	—	23.81	20.00	(5.00)	32.20

Q. 7. With the help of the following information prepare a Comparative Statement of Profit & Loss of Gopal Ltd.

Particulars	*Note No.*	*31.3.2021*	*31.3.2022*
Revenue from Operations		₹5,00,000	₹8,00,000
Cost of Materials Consumed		60% of Revenue from Operations	70% of Revenue from Operations
Other Expenses		20,000	24,000
Rate of Income Tax		50% of Net Profit before Tax	

[Ans. Profit after Tax 2022 ₹1,08,000; 2021 ₹90,000.]

Percentage (%) Change in :

Revenue from Operations	*Cost of Materials Consumed*	*Other Expenses*	*Profit before Tax*	*Profit after Tax*
60.00	86.67	20.00	20.00	20.00

Note While solving the question, figures of the year 2022 will be presented first and figures of the year 2021 thereafter

Q. 8. From the following information, prepare a Comparative Statement of Profit & Loss :

Particulars	*Note No.*	*31.3.2018*	*31.3.2017*
		₹	₹
Revenue from Operations		80,00,000	60,00,000
Materials Consumed		48,00,000	45,00,000
Other Expenses		10% of Materials Consumed	7.6% of Materials Consumed
Income Tax		40%	40%

[Ans. Profit after Tax 2018 ₹16,32,000; 2017 ₹6,94,800.]

Percentage (%) Change in :

Revenue from Operations	*Cost of Materials Consumed*	*Other Expenses*	*Profit before Tax*	*Profit after Tax*
33.33	6.67	40.35	134.89	134.89

Q. 9. Prepare a Comparative Statement of Profit & Loss with the help of the following information :

Particulars	*Note No.*	*31.3.2018*	*31.3.2017*
		₹	₹
Revenue from Operations		10,00,000	7,00,000
Cost of Materials Consumed		8,00,000	5,00,000
Employee Benefit Expenses		75,000	50,000
Other Expenses		20,000	10,000
Income Tax		50%	40%

[Ans. Profit after Tax 2018 ₹52,500; 2017 ₹84,000.]

Percentage (%) Change in :

Revenue from Operations	*Cost of Materials Consumed*	*Employee Benefit Expenses*	*Other Expenses*	*Profit before Tax*	*Profit After Tax*
42.86	60.00	50.00	100.00	(25.00)	(37.50)

Q. 10. Prepare a Comparative Statement of Profit & Loss from the following information :

Particulars	*Note No.*	*31.3.2020* ₹	*31.3.2019* ₹
Revenue from Operations		12,50,000	10,00,000
Purchase of Stock in Trade		7,70,000	4,20,000
Changes in Inventories		(1,20,000)	80,000
Other Expenses		52,000	30,000
Other Income		6,000	5,000

[Ans. Profit before Tax 2020 ₹5,54,000; 2019 ₹4,75,000.]

Percentage (%) Change in :

Revenue from Operations	*Other Income*	*Total Revenue*	*Purchase of Stock in Trade*	*Change in Inventories*	*Other Expenses*	*Profit before Tax*
25.00	20.00	24.98	83.33	(250.00)	73.33	16.63

Q. 11. From the following data, prepare statement of profits in Comparative form :

Particulars	*Note No.*	*31st March, 2020*	*31st March, 2019*
Revenue from Operations		₹10,00,000	₹8,00,000
Cost of Materials Consumed		58% of Revenue from Operations	60% of Revenue from Operations
Other Expenses		10% of Materials Consumed	15% of Materials Consumed
Income Tax Rate		40%	45%

[Ans. Profit after Tax 2020 ₹2,17,200; 2019 ₹1,36,400.]

Percentage (%) Change in :

Revenue from Operations	*Cost of Materials Consumed*	*Other Expenses*	*Profit before Tax*	*Profit after Tax*
25.00	20.83	(19.44)	45.97	59.24

Q. 12. From the following information, prepare a Comparative Statement of Profit:

Particulars	*Note No.*	*31.3.2020* ₹	*31.3.2019* ₹
Revenue from Operations		40,00,000	50,00,000

Finance Costs		25,00,000	30,00,000
Employee Benefit Expenses		5,00,000	5,00,000
Depreciation		2,70,000	3,00,000
Other Expenses		1,60,000	2,00,000

[Ans. Profit before Tax 2020 ₹5,70,000; 2019 ₹10,00,000.]

Percentage (%) Change in :

Revenue from Operations	*Finance Cost*	*Employee Benefit Expenses*	*Depreciation*	*Other Expenses*	*Profit before Tax*
(20.00)	(16.67)	—	(10.00)	(20.00)	(43.00)

ADDITIONAL QUESTIONS

Q. 1[illegible]. From the following Balance Sheets of Universe Ltd., as at 31st March 2022 & 2021 prepare a Comparative Balance Sheet :

Universe Ltd.
BALANCE SHEET
as at 31st March 2022 and 2021

Particulars	*Note No.*	*31.3.2022*	*31.3.2021*
1	2	3	4
I. EQUITY AND LIABILITIES :		₹	₹
(1) Shareholder's Funds :			
(*a*) Share Capital		20,00,000	15,00,000
(*b*) Reserves and Surplus		3,00,000	4,00,000
(2) Non-Current Liabilities :			
Long-term Borrowings		9,00,000	6,00,000
(3) Current Liabilities :			
Trade Payables		3,00,000	2,00,000
TOTAL		35,00,000	27,00,000
II. ASSETS :			
(1) Non-Current Assets			
(*a*) Fixed Assets			
(*i*) Tangible Assets		20,00,000	15,00,000
(*ii*) Intangible Assets		9,00,000	6,00,000
(2) Current Assets			
(*a*) Inventories		3,00,000	4,00,000
(*b*) Cash and Bank Balance		3,00,000	2,00,000
TOTAL		35,00,000	27,00,000

[Ans. Percentage Change in Share Capital 33.33; Reserve & Surplus (25); Non Current Liabilities 50; Current Liabilities 50; Tangible Assets 33.33; Intangible Assets 50; Inventories (25); Cash & Bank Balance 50. Total of Balance Sheet 29.63.]

Q. 14. From the following information, prepare a Comparative Balance Sheet of Depth Ltd.

Particulars	*31.3.2022* ₹	*31.3.2021* ₹
Share Capital	25,00,000	25,00,000
Fixed Assets	36,00,000	30,00,000
Reserves and Surplus	6,00,000	5,00,000
Investments	5,00,000	5,00,000
Long-term Loans	15,00,000	15,00,000
Inventory	4,00,000	7,00,000
Trade Receivables	6,00,000	5,00,000
Cash and Bank Balance	50,000	3,00,000
Trade Payables	5,50,000	5,00,000

[Ans. Percentage Change in Share Capital Nil; Reserves and Surplus 20.00; Non-Current Liabilities Nil; Current Liabilities 10.00; Fixed Assets 20.00; Investments Nil; Inventory (42.86); Trade Receivables 20.00; Cash & Bank Balance (83.33)]

Q. 15. Following are the summarized Balance Sheets of R.P. Ltd. Prepare a Comparative Balance Sheet :

Particulars	*Note No.*	*31.3.2022*	*31.3.2021*
I. EQUITY AND LIABILITIES :		₹	₹
1. Shareholder's Funds :			
(*a*) Share Capital		9,00,000	7,50,000
(*b*) Reserve & Surplus		2,25,000	1,50,000
2. Non-Current Liabilities			
Long term Borrowings		3,00,000	4,20,000
3. Current Liabilities			
(*a*) Short term Borrowings		4,05,000	4,50,000
(*b*) Trade Payables		1,50,000	1,35,000
TOTAL		19,80,000	19,05,000
II. ASSETS :			
1. Non Current Assets :			
Fixed Assets			
(*i*) Tangible Assets		10,40,000	8,00,000
(*ii*) Intangible Assets		2,00,000	4,00,000
2. Current Assets :			
(*a*) Inventories		6,40,000	5,80,000
(*b*) Cash and Bank Balance		1,00,000	1,25,000
TOTAL		19,80,000	19,05,000

[Ans. Percentage change in Share Capital 20.00; Reserves and Surplus 50.00; Non-Current Liabilities (28.57); Short term Borrowings (10.00); Trade Payables

11.11; Tangible Assets 30.00; Intangible Assets (50.00); Inventories 10.34; Cash and Bank Balance (20.00).]

Q. 16. Prepare a Comparative Statement of Profit & Loss with the help of following information :

	Note No.	2018-19 ₹	2019-20 ₹
Revenue from Operations		20,00,000	30,00,000
Expenses		12,00,000	21,00,000
Other Incomes		4,00,000	3,60,000
Income Tax		50%	50%

[**Ans.** Profit after Tax 2020 ₹6,30,000; 2019 ₹6,00,000.]

Percentage (%) Change in :

Revenue from Operations	*Other Income*	*Total Revenue*	*Expenses*	*Profit before Tax*	*Profit after Tax*
50.00	(10.00)	40.00	75.00	5.00	5.00

Note : While solving the question, figures of 2019-20 will be presented first.

Q. 17. From the following figures relating to R.P. Ltd., prepare a Comparative Statement of Profit & Loss showing the percentage increase/decrease in 2018 over 2017 :

	Note No.	2017-18 ₹	2016-17 ₹
Revenue from Operations		7,50,000	5,00,000
Other Incomes		15,000	20,000
Expenses		4,50,000	3,00,000
Income Tax		50,000	40,000

[**Ans.** Profit after Tax 2018 ₹2,65,000; 2017 ₹1,80,000.]

Percentage (%) Change in :

Revenue from Operations	*Other Income*	*Total Revenue*	*Expenses*	*Profit before Tax*	*Profit after Tax*
50.00	(25.00)	47.12	50.00	43.18	47.22

Q. 18. From the following information, prepare a Comparative Statement of Profit & Loss :

Particulars	*Note No.*	*2019-20* ₹	*2018-19* ₹
Revenue from Operations		40,00,000	50,00,000
Cost of Materials Consumed		20,00,000	30,00,000
Other Expenses		7,00,000	10,00,000
Other Income		1,00,000	2,00,000

[**Ans.** Profit before Tax 2020 ₹14,00,000; 2019 ₹12,00,000.]

Percentage (%) Change in :

Revenue from Operations	*Other Income*	*Total Revenue*	*Cost of Materials Consumed*	*Other Expenses*	*Profit before Tax*
(20.00)	(50.00)	(21.15)	(33.33)	(30.00)	16.67

Q. 19. Prepare a comparative Statement of Profit & Loss showing changes in the absolute figures and comment on the performance :

Particulars	*Note No.*	*2019-20* ₹	*2018-19* ₹
Revenue from Operations		18,00,000	13,20,000
Cost of Materials Consumed		13,40,000	10,00,000
Other Expenses		2,00,000	1,40,000
Income Tax Paid		40%	40%

[**Ans.** Profit after Tax 2020 ₹1,56,000; 2019 ₹1,08,000.]

Percentage (%) Change in :

Revenue from Operations	*Cost of Materials Consumed*	*Other Expenses*	*Total Expenses*	*Profit before Tax*	*Profit After Tax*
36.36	34.00	42.86	35.09	44.44	44.44

Q. 20. Items of Profit & Loss Statement for two financial years ending on 31st March are given below. You are required to prepare Comparative Statement of Profit and Loss :

Particulars	*Note No.*	*2019-20* ₹	*2018-19* ₹
Revenue from Operations		12,00,000	10,00,000
Cost of Materials Consumed		8,72,000	7,00,000
Other Expenses		10% of Materials Consumed	
Miscellaneous Incomes		20,000	15,000

[**Ans.** Profit before Tax 2020 ₹2,60,800; 2019 ₹2,45,000.]

Percentage (%) Change in :

Revenue from Operations	*Other Income*	*Total Revenue*	*Cost of Materials Consumed*	*Other Expenses*	*Profit Before Tax*
20.00	33.33	20.20	24.57	24.57	6.45

Q. 21. Prepare a Comparative Statement of Profit & Loss from the following information :

Particulars	*Note No.*	*2019-20*	*2018-19*
Revenue from Operations		₹6,00,000	₹4,00,000
Cost of Materials Consumed		70% of Revenue from Operations	60% of Revenue from Operations
Indirect Expenses		20% of Cost of Materials Consumed	25% of Cost of Materials Consumed
Income Tax		40% of Net Profit before Tax	40% of Net Profit before Tax

[Ans. Profit after Tax 2020 ₹57,600; 2019 ₹60,000.]

Percentage (%) Change in :

Revenue from Operations	*Cost of Materials Consumed*	*Other Expenses*	*Total Expenses*	*Profit before Tax*	*Profit after Tax*
50.00	75.00	40.00	68.00	(4.00)	(4.00)

Q. 22. Prepare a Comparative Statement of Profit from the following information:

Particulars	*Note No.*	*31st March 2020* ₹	*31st March 2019* ₹
Revenue from Operations		15,00,000	12,00,000
Purchase of Stock in Trade		10,00,000	7,00,000
Changes in Inventories		1,50,000	1,00,000
Other Expenses		8% of Revenue from Operations	10% of Revenue from Operations

[Ans. Profit after Tax 2020 ₹2,30,000; 2019 ₹2,80,000.]

Percentage (%) Change in :

Revenue from Operations	*Purchase of Stock in Trade*	*Changes in Inventories*	*Other Expenses*	*Total Expenses*	*Profit before Tax*
25.00	42.86	50.00	—	38.04	(17.86)

Q. 23. Prepare a comparative Statement of Profit of Varun Ltd. with the help of the following information :

Particulars	*Note No.*	*31st March 2020* ₹	*31st March 2019* ₹
Revenue from Operations		56,00,000	60,00,000
Purchase of Stock in Trade		36,00,000	40,00,000
Changes in Inventories		(4,00,000)	(2,50,000)
Employee Benefit Expenses		6,00,000	5,00,000
Other Expenses		80,000	1,00,000

[Ans. Profit before Tax 2020 ₹17,20,000; 2019 ₹16,50,000.]

Percentage (%) Change in :

Revenue from Operations	*Purchase of Stock in Trade*	*Changes in Inventories*	*Employee Benefit Expenses*	*Other Expenses*	*Profit before Tax*
(6.67)	(10.00)	(60.00)	20.00	(20.00)	4.24

Q. 24. From the following data, prepare a Statement of Profits in the comparative form :

Particulars	*Note No.*	*31.3.2020* ₹	*31.3.2019* ₹
Revenue from Operations		80,00,000	75,00,000
Purchase of Stock in Trade		40,00,000	36,00,000
Changes in Inventories		3,00,000	(2,00,000)
Other Expenses		6,00,000	2,00,000

[**Ans.** Profit before Tax 2020 ₹31,00,000; 2019 ₹39,00,000.]

Percentage (%) Change in :

Revenue from Operations	*Purchase of Stock in Trade*	*Changes in Inventories*	*Other Expenses*	*Total Expenses*	*Profit before Tax*
6.67	11.11	250.00	200.00	36.11	(20.51)

Hint : Change in Inventories :

2020	*2019*	*Absolute Change*	*% Change*
3,00,000	(2,00,000)	5,00,000	250.00

Q. 25. Prepare a Comparative Statement of Profit with the help of the following information :

Particulars	*Note No.*	*31-3-2020* ₹	*31-3-2019* ₹
Revenue from Operations		30,00,000	20,00,000
Purchase of Stock in Trade		16,00,000	12,00,000
Change in Inventories		(1,25,000)	2,50,000
Other Expenses		10% of Revenue from Operations	8% of Revenue from Operations

[**Ans.** Profit before Tax 2020 ₹12,25,000; 2019 ₹3,90,000.]

Percentage (%) Change in :

Revenue from Operations	*Purchase of Stock in Trade*	*Changes in Inventories*	*Other Expenses*	*Total Expenses*	*Profit before Tax*
50.00	33.33	(150.00)	87.50	10.25	214.10

Hint : Change in Inventories :

2020	*2019*	*Absolute Change*	*% Change*
(1,25,000)	2,50,000	(3,75,000)	(150.00)

Q. 26. Profit & Loss Statements for the years ended 31st March 2022 and 2021 :

Particulars	*Note No.*	*31-3-2022* ₹	*31-3-2021* ₹
Revenue from Operations		48,00,000	50,00,000
Finance Costs		27,50,000	30,00,000
Employee Benefit Expenses		5,00,000	4,00,000
Other Expenses		80,000	1,00,000
Income Tax		40%	35%

Calculate percentage changes from 2021 to 2022.

[**Ans.** Profit After Tax 2022 ₹8,82,000; 2021 ₹9,75,000.]

Percentage (%) Change in :

Revenue from Operations	*Employee Benefit Expenses*	*Finance Costs*	*Other Exp.*	*Profit before Tax*	*Profit after Tax*
(4.00)	25.00	(8.33)	(20.00)	(2.00)	(9.54)

Q. 27. Prepare a Comparative Statement of Profit & Loss from the following :

	Note No.	*31st March, 2022*	*31st March, 2021*
Revenue from Operations		40,00,000	30,00,000
Expenses		58% of Revenue from Operations	60% of Revenue from Operations

Interest on investments @ ₹2,00,000 and taxes payable @ 50%.

[**Ans.** Profit after Tax 2022 ₹9,40,000; 2021 ₹7,00,000.]

Percentage (%) Change in :

Revenue from Operations	*Other Income*	*Total Revenue*	*Expenses*	*Profit before Tax*	*Profit After Tax*
33.33	NIL	31.25	28.89	34.29	34.29

Q. 28. From the following information, prepare a Comparative Statement of Profit & Loss of Zee Ltd.:

	Note No.	*31-3-2022* ₹	*31-3-2021* ₹
Revenue from Operations		150% of Materials Consumed	120% of Materials Consumed
Materials Consumed		20,00,000	10,00,000
Other Expenses		20% of Materials Consumed	10% of Materials Consumed
Income Tax		40%	40%

[Ans. Profit after Tax 2022 ₹3,60,000; 2021 ₹60,000.]

Percentage (%) Change in :

Revenue from Operations	*Cost of Materials Consumed*	*Other Expenses*	*Total Expenses*	*Profit before Tax*	*Profit after Tax*
150.00	100.00	300.00	118.18	500.00	500.00

Q. 29. Prepare a Comparative Statement of Profit & Loss from the following information :

	Note No.	*31.3.2022* ₹	*31.3.2021* ₹
Revenue from Operations		50,00,000	40,00,000
Finance Costs		22,00,000	16,00,000
Employee Benefit Expenses		6,00,000	5,00,000
Other Expenses (5% of Revenue from Operations)			
Income Tax		40%	45%

[Ans. Profit after Tax 2022 ₹11,70,000; 2021 ₹9,35,000.]

Percentage (%) Change in :

Revenue from Operations	*Employee Benefit Expenses*	*Finance Costs*	*Other Expenses*	*Profit before Tax*	*Profit After Tax*
25.00	20.00	37.50	25.00	14.71	25.13

Q. 30. From the following Statement of Profit and Loss of Moontrack Ltd., for the years ended 31st March 2020 and 2019, prepare a 'Comparative Statement of Profit & Loss'.

Particulars	*Note No.*	*2019-20* ₹	*2018-19* ₹
Revenue from Operations		40,00,000	24,00,000
Other Incomes		24,00,000	18,00,000
Expenses		16,00,000	14,00,000

[Ans. Profit before Tax 2020 ₹48,00,000 and 2019 ₹28,00,000.]

Percentage (%) Change in :

Revenue from Operations	*Other Income*	*Total Revenue*	*Expenses*	*Profit before Tax*
66.67	33.33	52.38	14.29	71.43

Q. 31. Prepare Comparative Statement of Profit & Loss from the following :

Particulars	*Note No.*	*31.3.2022* ₹	*31.3.2021* ₹
Revenue from Operations		15,00,000	10,00,000

Expenses		10,50,000	6,00,000
Other Income		1,80,000	2,00,000

[**Ans.** Profit before Tax 2022 ₹6,30,000 and 2021 ₹6,00,000.]

Percentage (%) Change in :

Revenue from Operations	*Other Income*	*Total Revenue*	*Expenses*	*Profit before Tax*
50	(10)	40	75	5

Q. 32. From the following Statement of Profit and Loss of Star Ltd. for the years ended 31st March 2020 and 2019 prepare a comparative statement of Profit & Loss :

Particulars	*Note No.*	*31.3.2020* ₹	*31.3.2019* ₹
Revenue from Operations		20,00,000	16,00,000
Employee benefit Expenses		10,00,000	8,00,000
Other Expenses		1,00,000	2,00,000
Tax		50%	50%

[**Ans.** Profit after Tax 2020 ₹4,50,000 and 2019 ₹3,00,000.]

Percentage (%) Change in :

Revenue from Operations	*Employee Benefit Expenses*	*Other Expenses*	*Total Expenses*	*Profit before Tax*	*Profit after Tax*
25	25	(50)	10	50	50

Q. 33. From the following particulars, prepare a Comparative Balance Sheet of Rima Ltd. :

Particulars	*31.3.2022* ₹	*31.3.2021* ₹
Share Capital	33,00,000	32,00,000
Fixed Assets	40,00,000	35,00,000
6% Government Bonds	6,00,000	6,00,000
5% Debentures	16,00,000	14,00,000
Reserves and Surplus	2,00,000	5,00,000
Short Term Investments	4,00,000	5,00,000
Inventories	6,00,000	8,00,000
Trade Payables	6,00,000	5,00,000
Cash and Bank Balance	1,00,000	2,00,000

(From I.S.C. Guidelines)

SOLUTION:

COMPARATIVE BALANCE SHEET OF RIMA LTD.

as at 31st March 2022 and 2021

Particulars	*Note No.*	*31st March, 2022*	*31st March, 2021*	*Absolute Change (Increase/ Decrease) (Base Year - 2021)*	*Percentage (Increase/ Decrease) (Base Year - 2021)*
1		*2*	*3*	*4*	*5*
		₹	₹	₹	%
I. EQUITY AND LIABILITIES					
1. Shareholder's Funds					
(*a*) Share Capital		33,00,000	32,00,000	1,00,000	3.125
(*b*) Reserves and Surplus		2,00,000	5,00,000	(3,00,000)	(60)
2. Non-Current Liabilities					
Long-term borrowings		16,00,000	14,00,000	2,00,000	14.29
3. Current Liabilities					
Trade Payables		6,00,000	5,00,000	1,00,000	20
TOTAL		57,00,000	56,00,000	1,00,000	1.79
II. ASSETS					
1. Non-Current Assets					
(*a*) Fixed Assets		40,00,000	35,00,000	5,00,000	14.29
(*b*) Non-Current Investments		6,00,000	6,00,000	—	—
2. Current Assets					
(*a*) Current Investments		4,00,000	5,00,000	(1,00,000)	(20)
(*b*) Inventories		6,00,000	8,00,000	(2,00,000)	(25)
(*c*) Cash and Bank Balance		1,00,000	2,00,000	(1,00,000)	(50)
TOTAL		57,00,000	56,00,000	1,00,000	1.79

Q. 34. From the following data, prepare a Comparative Statement of Profit and Loss of Simon Ltd.

Date	*Particulars*	*31.3.2014*	*31.3.2013*
		₹	₹
	Revenue from Operations	15,00,000	12,00,000
	Other Income	30,000	20,000
	Cost of Materials consumed	7,00,000	5,50,000

(ISC, 2015)

[Ans. Percentage Change in :

Revenue from Operations	*Other Income*	*Total Revenue*	*Cost of Materials Consumed*	*Profit before Tax*
25	50	25.41	27.27	23.88

Q. 35. From the following information, prepare a Comparative Statement of Profit and Loss :

Particulars	*Note No.*	*31.3.2017*	*31.3.2016*
Revenue from operations		₹24,00,000	₹18,00,000
Other incomes (% of revenue from operations)		15%	25%
Expenses (% of revenue from operations)		60%	50%
Tax Rate		40%	40%

(C.B.S.E. 2018, Comptt.)

[Ans. Profit after tax : 2017 ₹7,92,000 and 2016 ₹8,10,000.

Percentage (%) Change in :

Revenue from Operations	*Other Income*	*Total Revenue*	*Expenses*	*Profit before and after Tax*
33.33	(20)	22.67	60	(2.22)

Q. 36. From the following information extracted from the Statement of Profit and Loss for the years ended 31st March, 2017 and 2018, prepare a Comparative Statement of Profit & Loss :

Particulars	*Note No.*	*2017-18*	*2016-17*
Revenue from operations		₹6,00,000	₹5,00,000
Other incomes (% of revenue from operations)		20%	20%
Employee benefit expenses (% of Total Revenue)		40%	30%
Tax Rate		50%	50%

(C.B.S.E. 2019, M.P.)

[Ans. Profit After Tax : 2017 ₹2,10,000 and 2018 ₹2,16,000.]

Precentage (%) Change in :

Revenue from Operations	*Other Income*	*Total Revenue*	*Employee Benefit Exp.*	*Profit Before and After Tax*
20	20	20	60	2.86

Q. 37. From the following information prepare Comparative Balance Sheet of X Ltd. :

Particulars	*31-3-2017* ₹	*31-3-2016* ₹
Share Capital	25,00,000	25,00,000
Reserves and Surplus	6,00,000	10,00,000
Long-term Borrowings	16,00,000	15,00,000
Current Liabilities	5,00,000	4,50,000
Fixed Assets	35,00,000	25,00,000
Investments (Non-Current)	10,50,000	15,00,000
Current Assets	6,50,000	14,50,000

(C.B.S.E. 2019; Delhi)

[**Ans.** Precentage Change in Share Capital Nil; Reserves and Surplus (40.00); Long term Borrowings 6.67; Current Liabilities 11.11; Fixed Assets 40.00; Non Current Investments (30.00); Current Investments (55.17); Total of Balance Sheet (4.59)]

Q. 38. Prepare a Comparative Statement of Profit and Loss of Cosmos Ltd. from the following information :

Particulars	*31.03.2019*	*31.03.2018*
Revenue from Operations	₹20,00,000	₹10,00,000
Purchases of stock-in-trade less	₹12,00,000	₹6,00,000
Change in Inventories of Stock-in-trade less	25% of purchases of stock-in-trade	20% of purchases of stock-in-trade
Other Expenses less	₹1,00,000	₹80,000
Tax Rate less	40%	40%

(I.S.C. 2020)

SOLUTION :

Cosmos Ltd.

COMPARATIVE STATEMENT OF PROFIT & LOSS

for the years ended 31st March 2018 and 2019

Particulars	*Note No.*	*2018-19*	*2017-18*	*Absolute Change (Increase or Decrease)*	*Percentage Change (Increase or Decrease)*
		₹	₹	₹	%
I. Revenue from Operations		20,00,000	10,00,000	10,00,000	100
II. *Less* : Expenses					
Purchase of Stock in Trade		12,00,000	6,00,000	6,00,000	100
Change in Inventories*		3,00,000	1,20,000	1,80,000	150
Other Expenses		1,00,000	80,000	20,000	25
Total Expenses		16,00,000	8,00,000	8,00,000	100
III. Profit before tax (I-II)		4,00,000	2,00,000	2,00,000	100
IV. *Less* : Tax		1,60,000	80,000	80,000	100
V. Profit after Tax (III-IV)		2,40,000	1,20,000	1,20,000	100

*Changes in Inventories means Opening Stock *less* Closing Stock.

Multiple Choice Questions

Choose the Best Alternate :

Q. 1. The most commonly used tools for financial analysis are :

(A) Comparative Statements
(B) Common Size Statements
(C) Accounting Ratios
(D) All of the above

Q. 2. Which of the following is not a tool for Analysis of Financial Statements :

(A) Cash Flow Statement (B) Trend Analysis

(C) Ratio Analysis (D) Balance Sheet

(C.B.S.E. 2020; Rajasthan)

Q. 3. Which one of the following items is not a tool used for financial analysis?

(A) Comparative Statements (B) Ratio Analysis

(C) Common Size Statements (D) Statement of Dividend Distribution

Q. 4. Which one of the following items is not a method/tool of analysis of financial statements?

(A) Trend Analysis (B) Statement of Affairs

(C) Cash Flow Statement (D) Comparative Statements

Q. 5. Which one of the following items is not a method/tool of analysis of financial statements?

(A) Accounting Ratio

(B) Break Even Point

(C) Statement of Receipts and Payments

(D) Fund Flow Statement

Q. 6. Which one of the following items is not a method/tool of analysis of financial statements?

(A) Fund Flow Statement (B) Common Size Statement

(C) Statement of Trade Receivables (D) Cash Flow Statement

Q. 7. Which of the following is the objective of comparative Statements?

(A) To make the data simpler and understandable

(B) To indicate the trend

(C) To help in forecasting

(D) All of the Above

Q. 8. Which of the following is device of comparative statements?

(A) Comparison expressed in terms of absolute data

(B) Comparison expressed in terms of percentages

(C) Comparison expressed in terms of ratios

(D) All of the Above

Q. 9. Comparative Balance Sheet :

(A) Provides a summarized view of the operations of the firm

(B) Presents the financial position of the firm

(C) Presents the change in various items of balance sheet

(D) None of the above

Q. 10. Comparative Statement of Profit & Loss provides information about :

(A) Rate of increase or decrease in revenue from operations

(B) Rate of increase or decrease in cost of revenue from operations

(C) Rate of increase or decrease in net profit
(D) All of the above

Q. 11. Which analysis depicts the relationship between two figures :
(A) Ratio Analysis
(B) Trend Analysis
(C) Cumulative figures and averages
(D) Dividend Analysis

Q. 12. In which analysis total cost are equal to total revenue from Operations :
(A) Trend Analysis
(B) Ratio Analysis
(C) Break-Even Point Analysis
(D) Cash Flow Statement Analysis

Q. 13. Fixed Assets of a company increased from ₹3,00,000 to ₹4,00,000. What the percentage of change?
(A) 25%
(B) 33.3%
(C) 20%
(D) 40%

Q. 14. A Company's current liabilities decreased from ₹4,00,000 to ₹3,00,000. What is the percentage of change?
(A) (25%)
(B) 33.3%
(C) 20%
(D) 25%

Q. 15. A company's working capital is ₹10 lakh (Negative balance) in the year 2018. It became ₹15 lakh (Positive balance) in the year 2019. What is the percentage of change?
(A) 150%
(B) 100%
(C) 250%
(D) 50%

Q. 16. A company's Revenue from Operations are ₹20,00,000; Cost of Revenue from Operations is ₹14,00,000 and indirect expenses are ₹2,00,000. What is the amount of Gross Profit?
(A) ₹18,00,000
(B) ₹4,00,000
(C) ₹ 8,00,000
(D) ₹6,00,000

Q. 17. Revenue from Operations ₹4,00,000; Cost of Revenue from Operations 60% of Revenue from Operations; Operating expenses ₹ 30,000 and rate of income tax is 40%. What will be amount of profit after tax?
(A) ₹64,000
(B) ₹78,000
(C) ₹52,000
(D) ₹96,000

Q. 18. Revenue from Operations ₹8,00,000; Gross Profit Ratio 32%; Indirect Exp. 10% of Gross Profit and income tax 40%. What will be the amount of profit after tax?
(A) ₹1,38,240
(B) ₹1,02,400
(C) ₹ 92,160
(D) ₹1,53,600

Q. 19. Revenue from Operations ₹4,00,000; Cost of Revenue from Operations 60% of Revenue from Operations, indirect expenses 15% of Gross Profit; Income Tax 40%. Calculate net profit after tax
(A) ₹64,000
(B) ₹54,400
(C) ₹81,600
(D) ₹96,000

Q. 20. Payment of Income Tax is considered as

(A) Direct Expenses (B) Indirect Expenses
(C) Operating Expenses (D) None of the Above

Q. 21. Interest on Loans is

(A) Direct Expenses (B) Indirect Expenses
(C) Operating Expenses (D) None of the Above

Q. 22. Revenue from Operations less cost of Revenue from Operations is called :

(A) Net Profit (B) Operating Profit
(C) Gross Profit (D) Total Profit

Q. 23. Which objective is not fulfilled by comparative Statement of Profit & Loss :

(A) To compare the items of Statement of Profit & Loss of two years
(B) To know the absolute changes in items of Statement of Profit & Loss
(C) To show the change in financial position
(D) To know the percentage changes in items of Statement of Profit & Loss

Q. 24. In comparative statements change in different items is presented in the form of ....

(A) Money Values
(B) Percentages
(C) Both Money Values and Percentages
(D) None of the above

Q. 25. Which of the following is not a form of presenting financial analysis :

(A) Absolute figure Comparison
(B) Ratio Method
(C) Cumulative figures and averages
(D) Annual Report

Q. 26. Which objective is not fulfilled by comparative financial statement :

(A) Indicate the extent of change in assets and liabilities
(B) Indicate the extent of change in items of Statement of Pofit & Loss
(C) Show effect of operative activities on assets and liabilities
(D) Show the direction of change in assets and liabilities

Q. 27. 'No profit no loss' point is called :

(A) Fund Flow Point (B) Cash Flow Point
(C) Trend Analysis (D) Break Even Point

Q. 28. Net profit is obtained by deducting .... from Gross Profit.

(A) Operating Expenses
(B) Non-Operating Exp.
(C) Operating and Non-Operating Exp.
(D) None of the Above

Q. 29. Amount left after deducting gross profit from Revenue from Operations is generally :

(A) Cost of Revenue from Operations
(B) Material consumed
(C) Opening Inventory + Purchases – Closing Inventory
(D) All of the above

Q. 30. What is gross profit + materials consumed?

(A) Purchases
(B) Revenue from Operations
(C) Opening Inventory
(D) Closing Inventory

Q. 31. Which analysis is considered more dynamic?

(A) Horizontal Analysis
(B) Vertical Analysis
(C) Internal Analysis
(D) External Analysis

(See Answers at the end of the book.)

12

Common Size Statements

Meaning : Common size statements are those in which individual figures are converted into percentages to some common base. Percentage of each individual item shows its relation to its respective total. This type of analysis is called Vertical Analysis since each accounting variable is analysed vertically. Common size statements may be prepared for balance sheet as well as statement of profit and loss.

Common size statements comprise of the following items :

(*i*) Absolute figures of individual items of Statement of Profit & Loss and Balance Sheet for two or more successive periods, and

(*ii*) Percentage to some common base. Normally, the figure of revenue from operations is taken as a base for the Statement of Profit & Loss items and the total of assets or equity & liabilities is taken as a base for the Balance Sheet items.

Purpose or Utility of Common Size Statements

(*i*) **To present the change in various items in relation to revenue from operations, total assets or total liabilities** : One of the major drawbacks of comparative financial statements is that they do not present the change in various items in relation to revenue from operations, total assets or total equity & liabilities. This drawback is removed through the preparation of common size statements.

(*ii*) **To establish a relationship** : Over a period, a relationship is established between various items of the statement of profit & loss to revenue from operations and various items of balance sheet to total assets or total liabilities. Significant conclusions can be drawn by studying the change in such a relationship. For example, if over the years it is established that cost of materials consumed constitute 40% of revenue from operations, an increase in this percentage will need immediate attention.

(*iii*) **To provide for a common base for comparison** : Common size statements provide for a common base for comparison. Financial statements of different firms can be converted into uniform common-size format irrespective of the size of individual items. Hence, they facilitate the comparison of profitability and financial position of two or more businesses over a period of time.

Preparation of Common Size Balance Sheet

Meaning of Common Size Balance Sheet :

A common size balance sheet is a statement in which total of assets or equity & liabilities is assumed to be equal to 100 and all the figures are expressed as percentage of the total. In other words, each asset is expressed as percentage to total assets and each item of equity & liability is expressed as percentage to total equity & liabilities.

Purpose or Utility of Common Size Balance Sheet :

(*i*) To analyse changes in individual items of balance sheet.

(*ii*) To establish the trend in various items of assets and liabilities.

(*iii*) To judge the relative financial soundness for different enterprises belonging to the same industry by preparing their common size balance sheets for different periods.

(*iv*) To assess the financial strategy adopted by different enterprises belonging to the same industry.

Format of Common Size Balance Sheet :

The format of Common Size Balance Sheet consists of five columns.

(*i*) First column for items of Balance Sheet.

(*ii*) Second column for amounts of different items of assests and equity & liabilities of current year's balance sheet.

(*iii*) Third column for amounts of different items of assets and equity & liabilities of previous year's balance sheet.

(*iv*) Fourth column for percentage of different items of current year's assets and equity & liabilities to total assets/liabilities of current year which are taken as 100.

(*v*) Fifth column for percentage of different items of previous year's assets and liabilities to total assets/liabilities of previous year, which are taken as 100.

Format of a Common Size Balance Sheet

COMMON SIZE BALANCE SHEET

as at 31st March, 2020 and 2019

Particulars	*Note No.*	*Absolute Amounts*		*Percentage of Balance Sheet Total*	
		*2020**	*2019*	*2020*	*2019*
		₹	₹	%	%
I. EQUITY AND LIABILITIES :					
1. Shareholder's Funds					
(*a*) Share Capital		. . .	. . .	. . .	. . .
(*b*) Reserve & Surplus		. . .	. . .	. . .	. . .
2. Non-Current Liabilities					
(*a*) Long term Borrowings		. . .	. . .	. . .	. . .
(*b*) Long-term Provisions		. . .	. . .	. . .	. . .
3. Current Liabilities					
(*a*) Short-term Borrowings		. . .	. . .	. . .	. . .
(*b*) Trade Payables		. . .	. . .	. . .	. . .
(*c*) Other Current Liabilities		. . .	. . .	. . .	. . .
(*d*) Short-term Provisions		. . .	. . .	. . .	. . .
		. . .	. . .	100	100

II. ASSETS :					
1. Non-Current Assets					
(*a*) Fixed Assets :					
(*i*) Tangible Assets		. . .	. . .	. . .	. . .
(*ii*) Intangible Assets		. . .	. . .	. . .	. . .
(*b*) Non-Current Investments		. . .	. . .	. . .	. . .
(*c*) Long-term Loans and Advances		. . .	. . .	. . .	. . .
2. Current Assets					
(*a*) Current Investments		. . .	. . .	. . .	. . .
(*b*) Inventories		. . .	. . .	. . .	. . .
(*c*) Trade Receivables		. . .	. . .	. . .	. . .
(*d*) Cash & Bank Balance		. . .	. . .	. . .	. . .
(*e*) Short-term Loans and Advances		. . .	. . .	. . .	. . .
(*f*) Other Current Assets		. . .	. . .	. . .	. . .
		. . .	. . .	100	100

*As per new format under Schedule III, Balance Sheet of Current Year should be presented first and of Previous Year thereafter.

ILLUSTRATION 1.

Prepare Common Size Balance Sheet of Oxford Ltd. from the following information : (₹ *in Lakhs)*

Particulars	*31.3.2022*	*31.3.2021*
	₹	₹
Equity Share Capital	16.00	16.00
Preference Share Capital	2.00	2.00
Reserves and Surplus	5.40	4.00
Non-Current Liabilities	14.40	14.00
Current Liabilities	7.20	4.00
Non-Current Assets	30.60	28.00
Current Assets	14.40	12.00

SOLUTION :

OXFORD LTD.

COMMON SIZE BALANCE SHEET

as at 31.3.2022 and 31.3.2021 (₹ *in Lakhs)*

Particulars	*Note No.*	*Absolute Amounts*		*Percentage of Balance Sheet Total*	
		2022	*2021*	*2022*	*2021*
		₹	₹	%	%
I. EQUITY AND LIABILITIES					
1. Shareholder's Funds :					
(*a*) Share Capital	1	18.00	18.00	40(i)	45(iv)
(*b*) Reserves & Surplus		5.40	4.00	12(ii)	10(v)
2. Non-Current Liabilities		14.40	14.00	32(iii)	35(vi)

3. Current Liabilities	7.20	4.00	16	10
	45.00	40.00	100	100
II. ASSETS				
1. Non-Current Assets	30.60	28.00	68	70
2. Current Assets	14.40	12.00	32	30
	45.00	40.00	100	100

Working Notes :

		2022	*2021*
(1)	Share Capital :		
	Equity Share Capital	16.00	16.00
	Preference Share Capital	2.00	2.00
		18.00	18.00

(2) All percentages will be calculated on the basis of total of Balance Sheet.

Hence, in 2022 percentages will be based on ₹45 Lakhs.
in 2021 percentages will be based on ₹40 Lakhs.

Thus, (*i*) $\frac{18}{45} \times 100 = 40\%$ (*ii*) $\frac{5.40}{45} \times 100 = 12\%$

(*iii*) $\frac{14.40}{45} \times 100 = 32\%$ (*iv*) $\frac{18}{40} \times 100 = 45\%$

(*v*) $\frac{4}{40} \times 100 = 10\%$ (*vi*) $\frac{14}{40} \times 100 = 35\%$

and so on.

ILLUSTRATION 2.

From the following data, prepare a Common Size Balance Sheet of Teak Wood Ltd. :

Particulars	*31.3.2022*	*31.3.2021*
	₹	₹
Share Capital	3,00,000	2,40,000
Reserve and Surplus	80,000	70,000
Trade Payables	1,00,000	1,10,000
Trade Receivables	1,90,000	1,80,000
Short Term Provisions	40,000	15,000
Fixed Assets	2,90,000	2,30,000
Long Term Provisions	80,000	65,000
Current Investments	10,000	8,000
Inventory	1,01,000	72,000
Cash and Bank Balance	9,000	10,000

(I.S.C. 2014 Modified)

SOLUTION :

Teak Wood Ltd.
COMMON SIZE BALANCE SHEET
as at 31st March, 2022 and 2021

Particulars	*Note No.*	*Absolute Amounts*		*Percentage of Balance Sheet Total*	
		2022	*2021*	*2022*	*2021*
		₹	₹	%	%
I. EQUITY AND LIABILITIES:					
1. Shareholder's Funds					
(*a*) Share Capital		3,00,000	2,40,000	50.00	48.00
(*b*) Reserve and Surplus		80,000	70,000	13.33	14.00
2. Non Current Liabilities					
Long term Provisions		80,000	65,000	13.33	13.00
3. Current Liabilities					
(*a*) Trade Payables		1,00,000	1,10,000	16.67	22.00
(*b*) Short term Provisions		40,000	15,000	6.67	3.00
TOTAL		6,00,000	5,00,000	100.00	100.00
II. ASSETS :					
1. Non Current Assets :					
(*a*) Fixed Assets		2,90,000	2,30,000	48.33	46.00
2. Current Assets :					
(*a*) Current Investments		10,000	8,000	1.67	1.60
(*b*) Inventory		1,01,000	72,000	16.83	14.40
(*c*) Trade Receivables		1,90,000	1,80,000	31.67	36.00
(*d*) Cash & Bank Balance		9,000	10,000	1.50	2.00
TOTAL		6,00,000	5,00,000	100.00	100.00

ILLUSTRATION 3.

From the following data, prepare a Common Size Balance Sheet of Palms Ltd. as at 31st March, 2018 :

(All calculations up to two decimal places)

Particulars	*31.03.2018*
	₹
Share Capital	24,00,000
Trade Payables	2,40,000
Fixed Assets (Tangible)	20,00,000
Fixed Assets (Intangible)	2,00,000
Reserves and Surplus	3,60,000
Cash and Bank Balances	8,00,000
Short-term Loans and Advances	2,00,000
Short-term Borrowings	40,000
Long-term Borrowings	1,60,000

(I.S.C. 2019)

SOLUTION :

COMMON SIZE BALANCE SHEET OF PALMS LTD.

As at 31st March, 2018

Particulars	*Note No.*	*31.03.2018* ₹	*% to Balance Sheet Total*
		₹	
I. EQUITY AND LIABILITIES :			
1. **Shareholder's Funds**			
(*a*) Share Capital		24,00,000	75.00
(*b*) Reserves & Surplus		3,60,000	11.25
2. **Non-Current Liabilities**			
Long-term Borrowings		1,60,000	5.00
3. **Current Liabilities**			
(*a*) Short-term borrowings		40,000	1.25
(*b*) Trade Payables		2,40,000	7.50
TOTAL		32,00,000	100
II. ASSETS :			
1. **Non-Current Assets**			
Fixed Assets			
(*i*) Tangible		20,00,000	62.50
(*ii*) Intangible		2,00,000	6.25
2. **Current Assets**			
(*a*) Cash & Bank Balances		8,00,000	25.00
(*b*) Short-term loans and advances		2,00,000	6.25
TOTAL		32,00,000	100

Preparation of Common Size Statement of Profit & Loss

Meaning of Common Size Statement of Profit & Loss :

A common size statement of profit & loss is a statement in which the figure of revenue from operations is assumed to be equal to 100 and all other figures are expressed as percentage of revenue from operations.

Purpose or Utility of Common Size Statement of Profit & Loss :

(*i*) To establish a relationship between individual items of statement of profit & loss and revenue from operations.

Since each item in a common size statement of profit & loss is shown as percentage of revenue from operations, a relationship can be established between each item of statement of profit & loss and volume of revenue from operations. The increase in revenue from operations will certainly increase selling expenses and not the administrative expenses. Administrative expenses may go up only if the revenue from operations increase to a considerable extent. In case the revenue from operations decline, the selling expenses should be reduced at once. Hence, a relationship is established between revenue from operations and other items of the statement of profi

& loss and such a relationship is helpful in analysing the increase or decrease in the percentage of each item.

(*ii*) To analyse changes in individual items of statement of profit & loss in relationship to revenue from operations.

(*iii*) To judge the relative efficiency of cost items of the two or more firms belonging to the same industry.

Format of Common Size Statement of Profit & Loss :

The format of Common Size Statement of Profit & Loss consists of five columns:

(*i*) First Column for items of Statement of Profit & Loss.

(*ii*) Second Column for amounts of different items (*i.e.*, Income/Expenses) of statement of profit & Loss for the current year.

(*iii*) Third Column for amounts of different items (*i.e.*, Income/Expenses) of statement of profit & Loss for the previous year.

(*iv*) Fourth Column for percentage of different items of statement of profit & Loss for the current year to Revenue from Operations of the current year, which are taken at 100.

(*v*) Fifth Column for percentage of different items of statement of profit & Loss for the previous year to Revenue from Operations of the previous year, which are taken at 100.

Format of a Common Size Statement of Profit & Loss

COMMON SIZE STATEMENT OF PROFIT & LOSS

for the years ended 31st March, 2020 and 2019

Particulars	*Note No.*	*Absolute Amounts*		*Percentage of Revenue from Operations*	
		2019-20	*2018-19*	*2019-20*	*2018-19*
		₹	₹	%	%
I. Revenue from Operations		...	...	100	100
II. *Add* : Other Incomes		...	...	...	...
III. Total Revenue (I + II)		...	...	...	...
IV. *Less* : Expenses :					
Cost of Materials Consumed		...	...	...	...
Purchase of Stock in Trade		...	...	...	...
Changes in Inventories of Finished Goods, Work-in-Progress and Stock in Trade		...	...	...	...
Employee Benefit Exp.		...	...	...	...
Finance Costs		...	...	...	...
Depreciation and amortization Exp.		...	...	...	...

Other Expenses					
Total Expenses					
V. Profit before Tax (III – IV)		(. . .)	(. . .)	( )	( )
VI. *Less* : Tax					
VII. Profit after Tax (V – VI)					

ILLUSTRATION 4

Prepare a Common Size Statement of Profit & Loss from the following :

Particulars	*Note No.*	*31-3-2018*	[illegible]
		₹	₹
Revenue from Operations		12,00,000	10,00,000
Cost of Materials Consumed		6,60,000	[illegible]
Employee Benefit Expenses		1,20,000	[illegible]
Other Expenses		96,000	[illegible]

SOLUTION: COMMON SIZE STATEMENT OF PROFIT & LOSS
for the years ended 31st March 2018 and 2017

Particulars	*Note No.*	*Absolute Amounts*		*Percentage of Revenue from Operations*	
		2017-18	*2016-17*	*2017-18*	[illegible]
		₹	₹	%	%
I. Revenue from Operations		12,00,000	10,00,000	100	[illegible]
II. *Less* : Expenses					
Cost of Materials Consumed		6,60,000	6,00,000	$55^{(1)}$	[illegible]
Employee Benefit Exp.		1,20,000	1,20,000	$10^{(2)}$	[illegible]
Other Expenses		96,000	50,000	$8^{(3)}$	[illegible]
Total Expenses		8,76,000	7,70,000	73	[illegible]
III. Profit before Tax (I – II)		3,24,000	2,30,000	27	[illegible]

All percentages will be calculated on the basis of Revenue from Operations. Calculation of percentages is as follows :

Year 2017-18	Year 2016-17
Notes : (1) $\frac{6,60,000}{12,00,000} \times 100 = 55\%$	(4) $\frac{6,00,000}{10,00,000} \times 100 = 60\%$
(2) $\frac{1,20,000}{12,00,000} \times 100 = 10\%$	(5) $\frac{1,20,000}{10,00,000} \times 100 = 12\%$
(3) $\frac{96,000}{12,00,000} \times 100 = 8\%$	(6) $\frac{50,000}{10,00,000} \times 100 = 5\%$

and so on.

ILLUSTRATION

Prepare a Common Size Statement of Profit & Loss from the following and interpret the same.

STATEMENT OF PROFIT AND LOSS

	Note No.	*31st March 2018*	*31st March 2017*
		₹	₹
Revenue from Operations		25,00,000	20,00,000
Other Income		1,00,000	1,00,000
Cost of Materials Consumed		17,00,000	14,00,000
Finance Costs		2,00,000	1,60,000
Other Expenses		1,00,000	1,40,000

SOLUTION: COMMON SIZE STATEMENT OF PROFIT & LOSS
for the years ended 31st March 2018 and 2017

Particulars	*Note No.*	*Absolute Amounts*		*Percentage of Revenue from Operations*	
		2017-18	*2016-17*	*2017-18*	*2016-17*
		₹	₹	%	%
I. Revenue from Operations		25,00,000	20,00,000	100	100
II. Other Incomes		1,00,000	1,00,000	4	5
III. Total Revenue (I + II)		26,00,000	21,00,000	104	105
IV. *Less*: Expenses					
Cost of Materials Consumed		17,00,000	14,00,000	68	70
Finance Costs		2,00,000	1,60,000	8	8
Other Expenses		1,00,000	1,40,000	4	7
Total Expenses		20,00,000	17,00,000	80	85
V. Profit before Tax (III – IV)		6,00,000	4,00,000	24	20

All percentages will be calculated on the basis of Total Revenue. Calculation of percentages is as follows :

Note : (1) $\frac{1,00,000}{25,00,000} \times 100 = 4\%$ (4) $\frac{1,00,000}{20,00,000} \times 100 = 5\%$

(2) $\frac{17,00,000}{25,00,000} \times 100 = 68\%$ (5) $\frac{14,00,000}{20,00,000} \times 100 = 70\%$

(3) $\frac{2,00,000}{25,00,000} \times 100 = 8\%$ (6) $\frac{1,60,000}{20,00,000} \times 100 = 8\%$

and so on.

Interpretation : The above statement reveals the following :

(*i*) Cost of materials consumed has reduced by 2% in the year 2017-18. This is due to reduction in the cost of raw materials.

(*ii*) Total expenses have decreased from 85% to 80%. As a result, profit before tax has increased from 20% to 24%. It may be concluded that the company has worked more efficiently in the year 2017-18 as compared to 2016-17.

ILLUSTRATION 6.

Prepare Common Size Statement of Profit & Loss from the following information:

	Note No.	*31.3.2022*	*31.3.2021*
		₹	₹
Revenue from Operations		40,00,000	25,00,000
Purchase of Stock in Trade		33,60,000	18,50,000
Changes in Inventories		(2,00,000)	1,50,000
Other Expenses		1,20,000	1,00,000
Other Income		1,60,000	50,000

SOLUTION :

COMMON SIZE STATEMENT OF PROFIT & LOSS

for the years ended 31st March 2022 and 2021

Particulars	*Note No.*	*Absolute Amounts*		*Percentage of Revenue from Operations*	
		2021-22	*2020-21*	*2021-22*	*2020-21*
		₹	₹	%	%
I. Revenue from Operations		40,00,000	25,00,000	100	100
II. *Add* : Other Income		1,60,000	50,000	4	2
III. Total Revenue (I + II)		41,60,000	25,50,000	104	102
IV. *Less* : Expenses					
Purchase of Stock in Trade		33,60,000	18,50,000	84	74
Changes in Inventories		(2,00,000)	1,50,000	(5)	6
Other Expenses		1,20,000	1,00,000	3	4
Total Expenses		32,80,000	21,00,000	82	84
V. Profit before Tax (III – IV)		8,80,000	4,50,000	22	18

ILLUSTRATION 7.

Prepare a Common Size Statement of Profit & Loss of AB Ltd. with the help of the following information :

	Note No.	*31.3.2019*	*31.3.2020*
		₹	₹
Revenue from Operations		20,00,000	30,00,000
Expenses		17,00,000	25,08,000
Other Incomes		2,00,000	4,00,000
Income Tax		35%	40%

SOLUTION :

COMMON SIZE STATEMENT OF PROFIT & LOSS
for the year ended 31st March 2020 and 2019

Particulars	*Note No.*	*Absolute Amounts*		*Percentage of Revenue from Operations*	
		2019-20	*2018-19*	*2019-20*	*2018-19*
		₹	₹	%	%
I. Revenue from Operations		30,00,000	20,00,000	100.00	100.00
II. Other Incomes		4,00,000	2,00,000	13.33	10.00
III. Total Revenue (I + II)		34,00,000	22,00,000	113.33	110.00
IV. *Less* : Expenses		25,08,000	17,00,000	83.60	85.00
V. Profit before Tax (III – IV)		8,92,000	5,00,000	29.73	25.00
VI. *Less* : Tax		3,56,800	1,75,000	11.89	8.75
VII. Profit after Tax		5,35,200	3,25,000	17.84	16.25

Note : Figures of the year 2019-20 will be presented first in comparison to 2018-19.

ILLUSTRATION 8

From the following data, prepare a Common Size Statement of Profit & Loss of Pitambar Ltd.

Particulars	*31.03.2016*	*31.03.2015*
	₹	₹
Revenue from Operations (% of Other Income)	200%	200%
Other Income	2,00,000	1,50,000
Cost of Materials consumed (% of Operating Revenue)	60%	50%
Other Expenses (% of Material Cost)	10%	20%
Tax Rate	30%	30%

(ISC Sample Paper, 2017)

SOLUTION : COMMON SIZE STATEMENT OF PROFIT & LOSS
for the years ended 31st March 2016 and 2015

Particulars	*Note No.*	*Absolute Amounts*		*Percentage of Revenue from Operations*	
		2015-16	*2014-15*	*2015-16*	*2014-15*
		₹	₹	%	%
I. Revenue from Operations		4,00,000	3,00,000	100	100
II. *Add* : Other Income		2,00,000	1,50,000	50	50
III. Total Revenue (I + II)		6,00,000	4,50,000	150	150
IV. *Less* : Expenses					
Cost of Materials Consumed		2,40,000	1,50,000	60	50
Other Expenses		24,000	30,000	6	10
Total Expenses		2,64,000	1,80,000	66	60

V. Profit before Tax (III – IV)		3,36,000	2,70,000	84	90
VI. *Less* : Tax		1,00,800	81,000	25.2	27
VII. Profit after Tax (V – VI)		2,35,200	1,89,000	58.8	63

ILLUSTRATION 9.

From the following information, prepare a Common Size Statement of Profit and Loss of Prudence Ltd. for the year ending 31st March, 2017 :

Particulars	*31.03.2017*
	₹
Revenue from Operations	20,00,000
Purchases	15,00,000
Changes in inventories	1,00,000
Other Income (Dividend received)	40,000
Depreciation and Amortization Expenses	60,000
Tax Rate @40%	

(I.S.C. 2018)

SOLUTION

COMMON SIZE STATEMENT OF PROFIT & LOSS OF PRUDENCE LTD.

for the year ending 31st March, 2017

Particulars	*Note No.*	*Absolute Amounts*	*Percentage to Revenue from Operations*
		₹	%
I. Revenue from Operations		20,00,000	100
II. Other Income (Dividend received)		40,000	2
III. Total Revenue (I + II)		20,40,000	102
IV. *Less* : Expenses			
Purchases		15,00,000	75
Changes in inventories		1,00,000	5
Depreciation and Amortization Expenses		60,000	3
Total Expenses		16,60,000	83
V. Profit before Tax (III – IV)		3,80,000	19
VI. *Less* : Tax		(1,52,000)	7.6
VII. Profit after Tax (V – VI)		2,28,000	11.4

Trend Percentage Analysis

Trend percentages are very useful in making comparative study of the financia statements for a number of years. These indicate the direction of movement over a lon time and help an analyst of financial statements to form an opinion as to whethe favourable or unfavourable tendencies have developed. This helps in future forecasts of various items.

For calculating trend percentages any year may be taken as the 'base year'. Each item of base year is assumed to be equal to 100 and on that basis the percentage of each item of each year is calculated. For example :

	2019	*2020*	*2021*	*2022*
Revenue from Operations (₹)	2,00,000	2,50,000	2,80,000	3,00,000
Trend percentage assuming 2019 as base year	100	125	140	150

Trend Percentages have been calculated as follows :

$$2020 : \frac{2,50,000}{2,00,000} \times 100 = 125$$

$$2021 : \frac{2,80,000}{2,00,000} \times 100 = 140$$

$$2022 : \frac{3,00,000}{2,00,000} \times 100 = 150$$

ILLUSTRATION 10

Calculate the trend percentages from the following information taking year ending 2015 as the base year :

Current Assets	*As at 31st March*			
	2019	*2020*	*2021*	*2022*
	₹	₹	₹	₹
Inventory	1,00,000	1,25,000	1,40,000	1,50,000
Trade Receivables	50,000	60,000	75,000	1,00,000
Cash and Bank Balance	10,000	15,000	25,000	20,000
Other Current Assets	40,000	30,000	60,000	50,000
	2,00,000	2,30,000	3,00,000	3,20,000

SOLUTION :

COMPARATIVE BALANCE SHEETS

as at 31st March, 2022

Current Assets	*Absolute Amounts*				*Trend Percentages*			
	2019	*2020*	*2021*	*2022*	*2019*	*2020*	*2021*	*2022*
	₹	₹	₹	₹	%	%	%	%
Inventory	1,00,000	1,25,000	1,40,000	1,50,000	100	125	140	150
Trade Receivables	50,000	60,000	75,000	1,00,000	100	120	150	200
Cash and Bank Balance	10,000	15,000	25,000	20,000	100	150	250	200
Other Current Assets	40,000	30,000	60,000	50,000	100	75	150	125
	2,00,000	2,30,000	3,00,000	3,20,000	100	115	150	160

Short Answer Questions

(Questions Carrying 1 Mark)

Q. 1. What are Common Size Statements?

Ans. Common size statements express all items of a financial statement as a percentage of some common base such as revenue from operations for profit and loss statement and total assets for balance sheet.

Q. 2. What is the meaning of Common Size Balance Sheet? *(ISC 2016)*

Ans. A common size balance sheet is a statement in which total of assets or equity & liabilities is assumed to be equal to 100 and all the figures are expressed as percentage of the total.

Q. 3. What is the meaning of Common Size Statement of Profit & Loss?

Ans. A common size statement of profit & loss is a statement in which the figure of revenue from operations is assumed to be equal to 100 and all other figures are expressed as percentage of revenue from operations.

Short Answer Questions

(Questions Carrying 2 Marks)

1. Give any two objectives of preparing Common Size Statements. *(ISC, 2015)*
2. Give any two uses of Common Size Statements.
3. Give two objectives of a Common Size Balance Sheet.
4. Give two objectives of a Common Size Statement of Profit & Loss.
5. Give a format of Common Size Balance Sheet of a company for two years.
6. Give a format of Common Size Statement of Profit & Loss for two years.
7. Take a few imaginary figures and prepare a Common Size Statement of Profit & Loss for two years.
8. What is meant by Trend Percentage Analysis?

PRACTICAL QUESTIONS

(Q. Nos. 1 to 10 are strictly in the serial order of Illustrations)

Q. 1. Prepare Common Size Balance Sheet of Vishal Paper Ltd. from the following information :

Particulars	*31.3.2022* ₹	*31.3.2021* ₹
Share Capital	21,00,000	21,00,000
Reserves and Surplus	9,10,000	6,00,000
Non-Current Liabilities	24,45,000	20,40,000
Current Liabilities	15,45,000	12,60,000
Non Current Assets	43,40,000	36,00,000
Current Assets	26,60,000	24,00,000

[Ans.	31.3.2022 (%)	31.3.2021 (%)
Share Capital	30	35
Reserves and Surplus	13	10
Non Current Liabilities	34.93	34
Current Liabilities	22.07	21
Non Current Assets	62	60
Current Assets	38	40

The following balance sheets relate to Modern Computers Ltd. convert these into common size balance sheet and interpret the same :

BALANCE SHEETS

as at 31st March

Particulars	*Note No.*	*2022*	*2021*
		₹	₹
I. Equity and Liabilities :			
1. Shareholder's Funds :			
(*a*) Share Capital		3,00,000	3,00,000
(*b*) Reserves and Surplus		6,50,000	4,36,000
2. Non-Currrent Liabilities :			
Long-term Borrowings		2,50,000	2,00,000
3. Current Liabilities :			
(*a*) Trade Payables		2,85,000	2,40,000
(*b*) Short term Provisions		15,000	24,000
		15,00,000	12,00,000
II. Assets :			
1. Non-Current Assets :			
(*a*) Fixed Assets		5,00,000	5,00,000
(*b*) Non-Current Investments		3,10,000	1,96,000
2. Current Assets :			
(*a*) Inventory		3,69,000	2,58,000
(*b*) Trade Receivables		2,25,000	1,98,000
(*c*) Cash & Bank Balance		96,000	48,000
		15,00,000	12,00,000

[Ans.	2022 (%)	2021 (%)
Share Capital	20	25
Reserve & Surplus	43.33	36.33
Non Current Liabilities	16.67	16.67
Trade Payables	19	20
Short term Provisions	1	2

Fixed Assets	33.33	41.67
Non Current Investments	20.67	16.33
Inventory	24.6	21.5
Trade Receivables	15	16.5
Cash & Bank Balance	6.4	4

Q. 3. Prepare a Common Size Balance Sheet of *X* Ltd. from the following information : *(₹ in Lakhs)*

	31.3.2022	*31.3.2021*
Current Assets	28.80	22.80
Non-Current Investments	1.80	1.20
Fixed Assets	41.40	36.00
Share Capital	30.00	30.00
Reserves & Surplus	12.00	7.20
Non-Current Liabilities	12.60	12.00
Current Liabilities	17.40	10.80

[**Ans.** Year 2022 : Share Capital 41.67%; Reserve & Surplus 16.66%; Non-Current Liabilities 17.5%; Current Liabilities 24.17%; Fixed Assets 57.5%; Investments 2.5%; Current Assets 40%.]

Year 2021 : Share Capital 50%; Reserve & Surplus 12%; Non-Current Liabilities 20%; Current Liabilities 18%; Fixed Assets 60%; Investments 2%; Current Assets 38%.]

Q. 4. Prepare a Common Size Statement of Profit & Loss from the following :

	Note No.	*2017-18* ₹	*2016-17* ₹
Revenue from Operations		14,00,000	10,00,000
Cost of Materials Consumed		8,40,000	6,50,000
Finance Costs		1,40,000	80,000
Other Expenses		70,000	60,000

[**Ans.** % of Revenue from Operations	*2017-18*	*2016-17*
Cost of Materials Consumed	60%	65%
Finance Costs	10%	8%
Other Expenses	5%	6%
Profit before Tax	25%	21%

Q. 5. Convert the following particulars into Common Size Statement of Profit & Loss and interpret the changes in 2018 :

Particulars	*Note No.*	*31st March 2018* ₹	*31st March 2017* ₹
Revenue from Operations		18,00,000	15,00,000

Other Income		72,000	45,000
Cost of Materials Consumed		8,64,000	6,60,000
Employee Benefit Expenses		1,80,000	1,80,000
Other Expenses		54,000	1,05,000

[Ans.

	Percentage of Revenue from Operations	
	2017-18	2016-17
Other Income	4	3
Cost of Materials Consumed	48	44
Employee Benefit Expenses	10	12
Other Expenses	3	7
Profit before Tax	43	40

Q. 6. Prepare a Common Size Statement of Profit & Loss from the following information of *X* Ltd.

	Note No.	31st March 2018 ₹	31st March 2017 ₹
Revenue from Operations		60,00,000	40,00,000
Purchase of Stock in Trade		43,20,000	30,40,000
Changes in Inventories		1,20,000	(80,000)
Other Incomes		1,50,000	60,000
Other Expenses		3,60,000	2,00,000

[Ans.

	Percentage of Revenue from Operations	
	2018	2017
Other Income	2.5	1.5
Purchase of Stock in Trade	72	76
Changes in Inventories	2	(2)
Other Expenses	6	5
Profit before Tax	22.5	22.5

Q. 7. Prepare a Common Size Statement of Profit & Loss from the following :

	Note No.	31.3.2022	31.3.2021
Revenue from Operations		40,00,000	42,00,000
Other Income		30,000	25,200
Finance Costs		24,00,000	26,88,000
Other Expenses		1,60,000	1,51,200
Income Tax (40%)			

[Ans.

	Percentage of Revenue from Operations	
	2022	2021
Other Income	0.75	0.60

	60.00	64.00
Finance Costs	4.00	3.60
Other Expenses	36.75	33.00
Profit before Tax	22.05	19.80
Profit after Tax		

Q. 8. You are given the following information :

	Note No.	*31.3.2021* ₹	*31.3.2022* ₹
Revenue from Operations		60,00,000	65,00,000
Other Income		36,000	91,000
Cost of Materials Consumed		43,39,200	44,49,250
Finance Costs		9,15,600	9,64,600
Other Expenses		1,50,000	2,08,000

Prepare a Common Size Statement of Profit & Loss from the above.

[**Ans.**	*Percentage of Revenue from Operations*	
	2021-22	*2020-21*
Other Income	1.40	0.6
Materials Consumed	68.45	72.32
Finance Costs	14.84	15.26
Other Expenses	3.20	2.50
Profit before Tax	14.91	10.52

Hint : Figures of the year 2021-22 will be presented first.

Q. 9. Prepare a Common Size Statement of Profit & Loss from the following for the year ended 31st March 2022 :

	Note No.	₹
Revenue from Operations		15,00,000
Cost of Materials Consumed		7,50,000
Other Expenses		2,10,000
Interest on Investments		60,000
Tax Payable @ 40%		

[**Ans.**	*Percentage of Revenue from Operations*
Other Income	4
Cost of Materials Consumed	50
Other Expenses	14
Profit before Tax	40
Profit after Tax	24

Q. 10. Calculate the trend percentages from the following information taking year ending 2019 as the base year :

Current Liabilities	*As at 31st March* *2019*	*2020*	*2021*	*2022*
	₹	₹	₹	₹
Short-term Borrowings	2,00,000	3,00,000	4,00,000	5,00,000
Trade Payables	50,000	40,000	80,000	1,00,000
Other Current Liabilities	1,50,000	3,00,000	2,40,000	6,00,000
	4,00,000	6,40,000	7,20,000	12,00,000

[Ans.	*2019*	*2020*	*2021*	*2022*
	%	%	%	%
Short-term Borrowings	100	150	200	250
Trade Payables	100	80	160	200
Other Current Liabilities	100	200	160	400
Total	100	160	180	300]

ADDITIONAL QUESTIONS

Q. 11. From the following Balance Sheets of Sun Ltd., as at 31st March, 2022 prepare a common size Balance Sheet.

Sun Ltd.

BALANCE SHEET *as at 31st March, 2022*

Particulars	*Note No.*	*31.3.2022*
I. **EQUITY AND LIABILITIES :**		₹
(1) **Shareholder's Funds**		
(*a*) Share Capital		40,00,000
(*b*) Reserves & Surplus		6,00,000
(2) **Non-Current Liabilities**		
Long-term Borrowings		12,00,000
(3) **Current Liabilities**		
Trade Payables		2,00,000
TOTAL		60,00,000
II. **ASSETS :**		
(1) **Non-Current Assets**		
(*a*) Fixed Assets		
(*i*) Tangible Assets		40,00,000
(*ii*) Intangible Assets		2,00,000
(2) **Current Assets**		
(*a*) Inventories		12,00,000
(*b*) Cash and Bank Balance		6,00,000
TOTAL		60,00,000

[Ans. Share Capital 66.67%; Reserve & Surplus 10%; Non-Current Liabilities 20%; Current Liabilities 3.33%; Tangible Assets 66.67%; Intangible Assets 3.33%; Inventories 20%; Cash & Bank Balance 10%.]

Q. 12. Following are the Balance Sheets of Gopalsons Ltd. as at 31st March 2022 and 31st March 2021 :

Particulars	*Note No.*	*31.3.2022*	*31.3.2021*
		₹	₹
I. EQUITY AND LIABILITIES :			
1. Shareholder's Funds :			
(*a*) Share Capital		12,00,000	10,00,000
(*b*) Reserve & Surplus		3,00,000	3,00,000
2. Non-Current Liabilities		6,20,000	4,60,000
3. Current Liabilities		8,80,000	7,40,000
TOTAL		30,00,000	25,00,000
II. ASSETS :			
1. Non-Current Assets		23,00,000	20,00,000
2. Current Assets		7,00,000	5,00,000
TOTAL		30,00,000	25,00,000

You are required to prepare a common size Balance Sheet.

[Ans. Year 2022 : Share Capital 40%; Reserve & Surplus 10%; Non-Current Liabilities 20.67%; Current Liabilities 29.33%; Non-Current Assets 76.67%; Current Assets 23.33%.]

Year 2021 : Share Capital 40%; Reserve & Surplus 12%; Non-Current Liabilities 18.4%; Current Liabilities 29.6%; Non-Current Assets 80%; Current Assets 20%.]

Q. 13. From the following information, prepare a Common Size Balance Sheet and comment upon the changes :

Particulars	*31.3.2021*	*31.3.2022*
	₹	₹
Share Capital	6,60,000	7,20,000
Reserves and Surplus	7,92,000	17,28,000
Non-Current Liabilities	6,65,000	4,00,000
Trade Payables	9,90,000	16,52,000
Short term Provision	1,93,000	3,00,000
Fixed Assets	10,00,000	20,00,000
Inventories	8,20,000	12,60,000
Trade Receivables	14,15,000	14,00,000
Cash and Bank Balance	65,000	1,40,000

[Ans.	*2022*	*2021*
Share Capital	15.00	20.00
Reserve & Surplus	36.00	24.00
Non Current Liabilities	8.33	20.15

Trade Payables	34.42	30.00
Short term Provisions	6.25	5.85
Fixed Assets	41.67	30.30
Inventories	26.25	24.85
Trade Receivables	29.17	42.88
Cash & Bank Balance	2.91	1.97

Hint : Figures of 2022 will be presented first.

Q. 14. Prepare a common size Balance Sheet and comment on the financial position of *X* Ltd. and *Y* Ltd. The Balance Sheets of *X* Ltd. and *Y* Ltd. as at 31.3.2022 are given below:

Particulars	*Note No.*	*X Ltd.*	*Y Ltd.*
I. EQUITY AND LIABILITIES :		₹	₹
Shareholder's Funds		9,00,000	12,00,000
Non-Current Liabilities		4,00,000	3,50,000
Current Liabilities		2,00,000	2,50,000
TOTAL		15,00,000	18,00,000
II. ASSETS :			
Non-Current Assets		10,00,000	16,00,000
Current Assets		5,00,000	2,00,000
TOTAL		15,00,000	18,00,000

[**Ans.**	*X Ltd.*	*Y Ltd.*
Shareholder's Funds	60.00%	66.67%
Non-Current Liabilities	26.67%	19.44%
Current Liabilities	13.33%	13.89%
Non-Current Assets	66.67%	88.89%
Current Assets	33.33%	11.11%]

Q. 15. Prepare a Common Size Statement of Profit & Loss of *Y* Ltd. from the following information :

	Note No.	*31.3.2022* ₹	*31.3.2021* ₹
Revenue from Operations		18,00,000	15,00,000
Cost of Materials Consumed		10,86,300	9,24,000
Employee Benefit Expenses		2,75,760	2,50,650
Other Expenses		45,000	30,000

[**Ans.**	*% of Revenue from Operations*	
	2021-22	*2020-21*
Cost of Materials Consumed	60.35	61.6
Employee Benefit Expenses	15.32	16.71

Other Expenses	2.5	2.00
Total Expenses	78.17	80.31
Profit before Tax	21.83	19.69

Q. 16. Prepare a Common Size Statement of Profit & Loss from the following :

	Note No.	*31.3.2022* ₹	*31.3.2021* ₹
Revenue from Operations		48,00,000	30,00,000
Purchase of Stock in Trade		32,64,000	21,00,000
Changes in Inventories		(1,92,000)	(90,000)
Other Expenses		3,36,000	1,50,000
Other Income		72,000	60,000
Income Tax (40%)			

[Ans.	*% of Revenue from Operations*	
	2021-22	*2020-21*
Other Income	1.5	2
Purchase of Stock in Trade	68	70
Changes in Inventories	(4)	(3)
Other Expenses	7	5
Profit before Tax	30.50	30
Profit after Tax	18.30	18

Q. 17. Prepare a Common Size Statement of Profit & Loss of Vinod Paper Mills Ltd. from the following information :

(₹ in Lakhs)

	Note No.	*31.3.2022*	*31.3.2021*
Revenue from Operations		30.00	25.00
Finance Costs		11.25	8.95
Employee Benefit Expenses		3.30	3.00
Other Expenses		0.96	0.96
Gain on Sale of Land		—	0.35

[Ans.	*% of Revenue from Operations*	
	2022	*2021*
Other Income	—	1.40
Finance Costs	37.50	35.80
Employee Benefit Expenses	11.00	12.00
Other Expenses	3.20	3.84
Profit before Tax	48.30	49.76

Q. 18. Prepare a Common Size Statement of Profit & Loss from the following :

	Note No.	31.3.2022 ₹	31.3.2021 ₹
Revenue from Operations		54,00,000	45,00,000
Purchase of Stock in Trade		35,10,000	28,80,000
Changes in Inventories		1,08,000	(2,25,000)
Other Expenses		3,24,000	4,95,000
Income Tax		40%	35%

[Ans.	% of Revenue from Operations	
	2022	2021
Purchase of Stock in Trade	65	64
Changes in Inventories	2	(5)
Other Expenses	6	11
Profit before Tax	27	30
Profit after Tax	16.2	19.5

Q. 19. Prepare a Common Size Statement of Profit & Loss of Fine Fabrics Ltd. on the basis of the following particulars :

	Note No.	31.3.2022	31.3.2021
Revenue from Operations		20,00,000	16,00,000
Cost of Materials Consumed		9,60,000	7,20,000
Employee Benefit Expenses		1,60,000	1,60,000
Depreciation		1,20,000	1,20,000
Other Expenses (5% of Revenue from Operations)			
Income Tax		45%	40%

[Ans.	% of Revenue from Operations	
	2022	2021
Cost of Materials Consumed	48	45
Employee Benefit Expenses	8	10
Depreciation	6	7.5
Other Expenses	5	5
Profit betore Tax	33	32.5
Profit after Tax	18.15	19.5

Q. 20. (*a*) Give one use and one limitation of a Common Size Statement.

Ans. :

Use : It shows the changes in various items in relation to Revenue from Operations, Total Assets and Total Liabilities.

Limitation : It explains the percentage of each item to the total sum (Revenue from Operations, Total Assets and Total Liabilities) but does not express the changes of the items between the two periods.

(*b*) From the following particulars, prepare a Common Size Balance Sheet of Rima Ltd.

Particulars	*31.3.2022* ₹	*31.3.2021* ₹
Share Capital SF	33,00,000	32,00,000
Fixed Assets NCA	40,00,000	35,00,000
6% Government Bonds NCA	6,00,000	6,00,000
5% Debentures NCL	16,00,000	14,00,000
Reserves and Surplus SF	2,00,000	5,00,000
Short Term Investment CA	4,00,000	5,00,000
Inventories CA	6,00,000	8,00,000
Trade Payables CL	6,00,000	5,00,000
Cash and Bank Balance CA	1,00,000	2,00,000

(From I.S.C. Guidelines)

[illegible]

Common Size Balance Sheet of Rima Ltd.
as at 31st March, 2022 and 2021

Particulars	*Note No.*	*Absolute Amounts* *31.3.2022* ₹	 *31.3.2021* ₹	*Percentage of Balance Sheet Total* *31.3.2022* %	 *31.3.2021* %
I. **EQUITY AND LIABILITIES:**					
1. **Shareholder's Funds :**					
(*a*) Share Capital		33,00,000	32,00,000	57.89	57.14
(*b*) Reserves & Surplus		2,00,000	5,00,000	3.51	8.93
2. **Non-Current Liabilities :**					
Long-term Borrowings		16,00,000	14,00,000	28.07	25.00
3. **Current Liabilities :**					
Trade Payable		6,00,000	5,00,000	10.53	8.93
		57,00,000	56,00,000	100	100
II. **ASSETS :**					
1. **Non-Current Assets :**					
(*a*) Fixed Assets		40,00,000	35,00,000	70.17	62.50
(*b*) Non-current Investments		6,00,000	6,00,000	10.53	10.71
2. **Current Assets :**					
(*a*) Current Investments		4,00,000	5,00,000	7.02	8.93
(*b*) Inventories		6,00,000	8,00,000	10.53	14.29
(*c*) Cash & Bank Balance		1,00,000	2,00,000	1.75	3.57
		57,00,000	56,00,000	100	100

Q. 21. From the following particulars :

(*i*) Prepare a Comparative Statement of Profit & Loss of Prudence Ltd.

(*ii*) Prepare a Common Size Statement of Profit & Loss of Prudence Ltd.

Particulars	*2022*	*2021*
Revenue from Operations	₹5,00,000	₹3,00,000
Cost of materials consumed	60% of revenue from operations	50% of revenue from operations
Indirect Expenses	30% of cost of materials consumed	20% of cost of materials consumed
Tax Rate	40% of Net Profit before Tax	40% of Net Profit before Tax

(From I.S.C. Guidelines)

SOLUTION :

COMPARATIVE STATEMENT OF PROFIT AND LOSS
for the years ending 31st March, 2022 and 2021

Particulars	*Note No.*	*2021-22*	*2020-21*	*Absolute Change (Increase/ Decrease) Base year 2020-21*	*Percentage (Increase/ Decrease) Base year 2020-21*
1		2	3	4	5
I. Revenue from Operations		5,00,000	3,00,000	2,00,000	66.67
II. *Less* : Expenses :					
Cost of Materials Consumed		3,00,000	1,50,000	1,50,000	100.00
Indirect Expenses		90,000	30,000	60,000	200.00
Total Expenses		3,90,000	1,80,000	2,10,000	116.67
III. Profit before Tax (I – II)		1,10,000	1,20,000	(10,000)	(8.33)
IV. *Less* : Tax		(44,000)	(48,000)	(4,000)	(8.33)
V. Profit after Tax (III – IV)		66,000	72,000	(6,000)	(8.33)

COMMON SIZE STATEMENT OF PROFIT AND LOSS
for the years ending 31st March, 2022 and 2021

Particulars	*Note No.*	*Absolute Amounts*		*Percentage of Revenue from Operations*	
		2021-22	*2020-21*	*2021-22*	*2020-21*
I. Revenue from Operations		5,00,000	3,00,000	100	100
II. *Less* : Expenses :					
Cost of Materials Consumed		3,00,000	1,50,000	60.00	50.00
Indirect Expenses		90,000	30,000	18.00	10.00
Total Expenses		3,90,000	1,80,000	78.00	60.00

III. Profit before Tax (I – II)		1,10,000	1,20,000	22.00	40.00
IV. *Less* : Tax		(44,000)	(48,000)	8.80	16.00
V. Profit after Tax (III – IV)		66,000	72,000	13.20	24.00

Q. 22. From the information given below, prepare a Common Size Statement of Profit & Loss of Relay Ltd. :

Particulars	*31st March, 2014*	*31st March, 2013*
	₹	₹
Revenue from Operations	51,73,000	49,70,000
Other Income	35,000	40,000
Purchase of Stock-in Trade	40,50,000	33,20,000
Change in Inventories	(90,000)	1,00,000
Other Expenses	1,70,000	1,50,000

(ISC Sample Question Paper 2015)

[Ans.

Particulars	*Percentage of Revenue from Operations*	
	2013-14	*2012-13*
Other Income	0.68	0.80
Purchase of Stock in Trade	78.29	66.80
Changes in Inventories	(1.74)	2.01
Other Expenses	3.29	3.02
Profit before Tax	20.84	28.97

Q. 23. From the following data, prepare Common Size Balance Sheet of Mint Ltd.

Particulars	*31.3.2014*	*31.3.2013*
	₹	₹
Share Capital	1,50,000	1,20,000
Reserves and Surplus	30,000	30,000
Trade Payables	20,000	40,000
Fixed Tangible Assets	2,00,000	1,90,000

(ISC, 2015)

[Ans.

	Percentage of Balance Sheet Total	
	31-3-2014	*31-3-2013*
Share Capital	75	63.16
Reserves and Surplus	15	15.79
Trade Payables	10	21.05
Fixed Tangible Assets	100	100.00

Q. 24. From the following data, prepare a Common Size Statement of Profit and Loss of Nicholson Ltd.

Particulars	*31.03.2015*	*31.03.2014*
	₹	₹
Revenue from Operations	₹6,00,000	₹4,00,000
Cost of Materials consumed	60% of revenue from operations	50% of revenue from operations
Finance Cost	₹10,000	₹8,000
Tax Rate	40% of profit before tax	40% of profit before tax

(ISC 2016)

[Ans.

Particulars	*Percentage of Revenue from Operations*	
	2014-15	*2013-14*
Cost of material consumed	60	50
Finance cost	1.67	2
Profit before Tax	38.33	48
Profit after Tax	23.00	28.8

Q. 25. Prepare a Common Size Income Statement from the following :

Particulars	*31.3.2017*	*31.3.2016*
	₹	₹
Revenue from Operations	4,00,000	3,00,000
Expenses	50% of revenue from operations	60% of revenue from operations

Interest on investments ₹10,000 and taxes payable @ 40% for both the years.

(I.S.C. Specimen Question Paper, 2018)

[Ans.

Particulars	*Percentage of Revenue from Operations*	
	31-3-2017	*31-3-2016*
Other Income	2.5	3.33
Expenses	50	60
Profit before Tax	52.5	43.33
Profit after Tax	31.5	26

Multiple Choice Questions

Choose the Best Alternate :

Q. 1. Main objective of Common Size statement is :

(A) To present the changes in various items
(B) To provide for a common base for comparison
(C) To establish relationship between various items
(D) All of the Above

Q. 2. Main objective of Common Size Balance Sheet is :

(A) To establish relationship between revenue from operations and other items of statement of profit & loss
(B) To present changes in assets and liabilities
(C) To present changes in various items of income and expenses
(D) All of the Above

Q. 3. Common Size Statements are prepared

(A) In the form of Ratios
(B) In the form of Percentages
(C) In both of the Above
(D) None of the Above

Q. 4. Which of the following is untrue :

(A) Common size Balance Sheet
(B) Common size Statement of Profit & Loss
(C) Common size Cash Flow Statement
(D) None of the Above

Q. 5. Main objective of Common Size Statment of Profit & Loss is :

(A) To present changes in assets and liabilities
(B) To judge the financial soundness
(C) To establish relationship between revenue from operations and other items of statement of Profit & Loss
(D) All of the Above

Q. 6. In the Statement of Profit & Loss of a Common Size Statement :

(A) Figure of net revenue from operations is assumed to be equal to 100
(B) Figure of gross profit is assumed to be equal to 100
(C) Figure of net profit is assumed to be equal to 100
(D) Figure of assets is assumed to be equal to 100

Q. 7. In the Balance Sheet of a Common Size Statement:

(A) Figure of share capital is assumed to be 100
(B) Figure of current liabilities is assumed to be 100
(C) Figure of fixed assets is assumed to be 100
(D) Figure of total assets is assumed to be 100

Q. 8. Total assets of a firm are ₹20,00,000 and its fixed assets are ₹8,00,000. What will be the percentage of fixed assets on total assets?

(A) 60%
(B) 40%
(C) 29%
(D) 71%

Q. 9. If total assets of a firm are ₹8,20,000 and its fixed assets are ₹5,90,400, what will be the percentage of current assets on total assets?

(A) 42%
(B) 58%
(C) 28%
(D) 72%

Q. 10. If net revenue from operations of a firm are ₹1,20,000; cost of revenue from operations is ₹66,000 and operating expenses are ₹21,600, what will be the percentage of operating income on net revenue from operations?

(A) 55%
(B) 45%
(C) 73%
(D) 27%

Q. 11. If net revenue from operations of a firm are ₹15,00,000; Gross Profit is ₹9,00,000 and operating expenses are ₹75,000, what will be percentage of operating income on net revenue from operations?
(A) 45%
(B) 55%
(C) 35%
(D) 65%

Q. 12 Main objective of Trend Analysis is
(A) To make comparative study of the financial statements for a number of years
(B) To indicate the direction of movement
(C) To help in forecasts of various items
(D) All of the Above

Q. 13. What will be the trend percentage, if the Inventory of a firm is ₹2,00,000; ₹2,40,000; ₹3,00,000 and ₹4,00,000 respectively?
(A) 1, 1.2, 1.5, 2
(B) 10, 12, 15, 20
(C) 100, 120, 150, 200
(D) None of the Above

Q. 14. In a common size Balance Sheet, total liabilities are assumed to be equal to:
(A) 1
(B) 10
(C) 100
(D) 1,000

Q. 15. In a common size Statement of Profit & Loss, the amount of net revenue from operations is assumed to be equal to
(A) 1
(B) 10
(C) 100
(D) 1,000

Q. 16. The objective of common size Statement of Profit & Loss is not to
(A) Present Changes in Various items of incomes and expenses
(B) Judge the cost items
(C) Establish relationship between revenue from operations and other items of statement of profit & loss
(D) Judge the relative financial soundness for different enterprises

(See Answers at the end of the book.)

13

Cash-Flow Statement

A cash-flow statement is a statement showing inflows (receipts) and outflows (payments) of cash during a particular period of time. In other words, it is a summary of sources and applications of cash during a particular span of time. It analyses the reasons for changes in balance of cash between the two balance sheet dates. The term 'cash' here stands for cash and cash equivalents. A cash-flow statement includes only those items which affect cash.

A cash-flow statement can be for the past or can be projected for a future period.

Objectives of Cash Flow Statement

(*i*) To ascertain the sources (receipts) of Cash and Cash Equivalents from operating, investing and financing activities of the enterprise.

(*ii*) To ascertain the applications (payments) of Cash and Cash Equivalents under operating, investing and financing activities of the enterprise.

(*iii*) To ascertain the net change in Cash and Cash Equivalents i.e. the difference between sources and applications under the three activities between the dates of two consecutive Balance Sheets.

(*iv*) To highlight the major activities that have provided cash and that have used cash during a particular period and to show their effect on the overall cash balance.

Importance or Uses of Cash Flow Statement

The main objectives behind preparing a cash-flow statement can be laid down as under :—

(1) **Useful for Short-Term Financial Planning :** A cash-flow statement provides information for planning the short-term financial needs of the firm. Since it provides information regarding the sources and utilisation of cash during a period, it becomes easier for the management to assess whether it will have adequate cash to meet day-to-day expenses and pay the creditors in time, whether it will have sufficient cash to pay the long-term loans and interest thereon and whether it has enough cash to pay for the purchase of fixed assets or not.

(2) **Useful in Preparing the Cash Budget :** A cash flow statement prepared for the future period is helpful in preparing a cash budget. It informs the management about the surplus or deficit periods of cash, *i.e.*, in which months the receipts of cash will be in excess of payments and in which months the payments will be in excess of receipts. It helps in planning the investment of surplus cash in short-term investments and to plan short-term credit in advance for deficit periods.

(3) **Comparison with the Cash Budget** :— A cash budget is prepared at the commencement of the year, whereas a cash flow statement is prepared at the end of the year. A comparison between the two helps in ascertaining the extent to which the financial resources of the firm have been generated and used according to the plan. Causes of variances between the figures of two statements can be analysed and proper corrective measures may be taken.

(4) **Study of the Trend of Cash Receipts and Payments** :— A cash-flow statement reveals the speed at which the cash is being generated from trade receivables, inventory and other current assets and the speed at which the current liabilities are being paid. It enables the management to assess the true position of the cash in future.

(5) **It Explains the Deviations of Cash from Earnings** :— A firm may earn huge profits yet it may have paucity of cash or when it suffered a loss it may still have plenty of cash. A Cash flow statement explains the reasons for it.

(6) **Helpful in Ascertaining Cash Flow from Various Activities Separately** :— A Cash flow statement aims at highlighting the Cash flow from operating, investing and financing activities separately. It indicates how much cash has been generated or used in these activities.

(7) **Helpful in Making Dividend Decisions** :— The amount of dividend must be deposited in a separate 'Dividend Bank A/c' within 5 days of the declaration of such dividend. Hence the management takes the help of cash flow statement to ascertain the position of cash generated from operating activities which can be used for payment of dividend.

(8) **Test for the Managerial Decisions** :— It is a general rule that fixed assets should be purchased from funds raised from long-term sources like issue of shares, debentures, long-term loans etc. and these should be repaid out of cash generated from operating activities. The cash flow statement shows whether this policy has been properly followed by the management or not.

(9) **Useful to Outsiders** :— Cash flow statement helps the investors, debentureholders, bankers, lenders, supplier's of credit etc. to analyse the financial position of the enterprise and they can take proper decisions on the basis of such analysis.

Limitations of Cash-Flow Statement

(1) **Not suitable for Judging the Liquidity** :— It does not present true picture of the liquidity of a firm because the liquidity does not depend upon cash alone. Liquidity also depends upon those assets which can be converted into cash easily. Exclusion of these assets obstructs the true reporting of the ability of the firm to meet its liabilities when they become due for payment.

(2) **Possibility of Window-dressing** :— The possibility of window-dressing is higher in case of cash position in comparison to the working capital position of a firm. The cash balance can be easily manoeuvred by postponing purchases and other payments and by rapidly collecting cash from debtors before the balance sheet date. Hence, a fund-flow statement presents a more realistic picture than a cash-flow statement.

(3) **It ignores non-cash transactions :** -- Cash-flow statement ignores non-cash transactions like purchase of fixed assets by issuing shares or debentures, conversion of debentures into shares, issue of bonus shares. Hence, the true position of an enterprise cannot be judged by cash-flow statement.

(4) **It ignores the accrual concept of accounting :**— It is prepared on cash basis and hence ignores one of the basic concepts of accounting, namely accrual concept.

(5) **No substitute for an Income Statement :**— A Cash Flow Statement is not a substitute of Income Statement which takes into account both cash and non-cash items. Therefore, net cash flow does not mean net income of the business.

(6) **Historical in Nature :**— A cash flow statement is prepared on the basis of the past years. Hence, information revealed by it is historical in nature. Information revealed by it will be more useful if it is accompanied by the projected Cash Flow Statement.

Difference between Cash-Flow Statement and Cash Budget

There is not much difference between a cash-flow statement and a cash budget. The only difference is that a cash-flow statement is prepared for a past period whereas a cash budget is prepared for a future period. Cash-flow statement usually portray how cash was received and spent in the past period. Hence, it is of limited use as far as the future periods are concerned. A cash budget is therefore prepared showing how much cash is likely to be received and what will be the disbursements during a future period of time? Thus, a cash budget indicates in which months there will be surplus cash and in which months there will be deficiency of cash resources. The management can then take suitable decision to invest the surplus cash or make arrangement for the deficiency of cash at the required time.

Distinction between Cash Flow Statement and Income Statement

Basis of Distinction	*Cash Flow Statement*	*Income Statement (or Statement of Profit & Loss)*
1. **Nature**	It records sources and utilisation of cash.	It records revenues and expenses.
2. **Objective**	The purpose of cash flow statement is to provide information about cash flows from operating, investing and financing activities for a given period.	The purpose of income statement is to ascertain the net profit or loss for a given period.
3. **Information needed for Preparation**	It is prepared on the basis of two consecutive balance sheets and additional information.	It is prepared from the balances of nominal accounts and additional information.
4. **Scope**	It shows only the movement of cash i.e. cash inflows and cash outflows. Hence, its scope is limited.	It shows the result of all business transactions for a period. Hence, its scope is wide.

5. **Basis of Preparation**	It is prepared on cash basis of accounting.	It is prepared on accrual basis of accounting.
6. **Matching**	It matches the sources of cash with the utilisation of cash and hence discloses positive or negative cash flow from different activities.	It matches cost of goods sold and expenses with sales and other incomes and discloses net profit or loss.
7. **Timing of Preparation**	It is prepared after the preparation of financial statements.	It is not prepared from cash flow statement.
8. **Liquidity Vs Profitability**	It reveals liquidity position of the business.	It reveals profitability position of the business.
9. **Format**	Accounting Standard 3 (Revised) prescribes the format and contents of cash flow statement.	Schedule III of the Companies Act, 2013 has prescribed the format and contents of statement of profit and loss.
10. **Manipulation**	Manipulation of cash flow statement is not possible because it shows the actual balance of cash and cash equivalents at the end.	Manipulation of income statement is quite possible and it may show inflated income by overvaluation of inventory, reduced depreciation etc.

Procedure of Preparing Cash-Flow Statement

The Institute of Chartered Accountants of India has issued Accounting Standard (AS)–3 Revised, for preparing a cash flow statement. This Accounting Standard has been made mandatory in respect of accounting periods commencing on or after 1st April 2001, for certain enterprises. These enterprises are :

(*i*) Enterprises whose equity or debt securities are listed on a recognised stock exchange in India, and enterprises that are in the process of issuing equity or debt securities that will be listed on a recognised stock exchange in India.

(*ii*) All other commercial, industrial and business enterprises, whose turnover for the accounting period exceeds ₹50 Crores.

As such, the Cash flow statement has been prepared according to AS–3 Revised in this Chapter.

According to AS–3 Revised, the cash flow statement summarizes the cash inflows and cash outflows and the net changes (increase or decrease) in cash and cash equivalents resulting from operating, investing and financing activities of a firm during a period.

The following terms are used for preparing a cash flow statement :

Cash :— It comprises cash in hand and demand deposits with banks *i.e.*, deposits which are repayable by banks on demand.

Cash Equivalents :— These are short-term, highly liquid investments that are readily convertible into known amounts of cash and which present insignificant risk of changes in their values. Normally, an investment will be termed as cash equivalent only if it has a short maturity period, say three months or less, from the date of its acquisition. Examples of cash equivalents are treasury bills, commercial papers etc. which are purchased with cash that is in excess of immediate needs. Investment in shares are excluded from cash equivalents unless they are cash equivalent in reality. For example, the investment in preference shares of a company if they are redeemable within 3 months from the date of purchase will be included in cash equivalents, provided there is only an insignificant risk of failure of the company in repaying the amount at the date of maturity.

Thus, Cash and Cash Equivalents include the following :

(*i*) Cash in Hand

(*ii*) Cash at Bank

(*iii*) Short-term Investments or Marketable Securities

(*iv*) Cheques and Drafts on Hand

ISC Council's Instructions

(*i*) Bank Overdraft and Cash Credit will be considered as financing activity as they are short term borrowings. Henceforth, they will not be considered as cash and cash equivalents.

(*ii*) Current investments will be considered as part of working capital changes unless specified as marketable securities or short term investments.

Classification of Cash Flows :— According to AS–3 (Revised), a cash flow statement should be presented in a manner that it reports inflows and outflows of cash by classifying them into three categories, namely : operating, investing and financing activities. Classification of all activities into these three categories helps the users of cash flow statement to assess the effect of these activities on the cash and cash equivalents of the enterprise. Such information will be helpful in evaluating the relationship among these three activities. These three activities are explained as below:

(1) Cash Flows from Operating Activities :

Operating activities are the main revenue generating activities of an enterprise. As such, they include cash flows from those transactions and events which enter into the ascertainment of net profit or loss of the enterprise. Examples of Cash flows arising from operating activities are :

(*a*) Cash receipts from the sale of goods and rendering of services;

(*b*) Cash receipts from royalties, fees, commissions and other revenue;

(*c*) Cash receipts from Debtors and Bills Receivables;

(*d*) Cash payments for purchase of goods and services;

(*e*) Cash payments to Creditors and Bills Payable;

(*f*) Cash payment of wages, salaries and other payment to employees;

(*g*) Cash payments or refunds of income taxes unless they can be specifically identified with financing and investing activities.

(2) Cash Flows from Investing Activities :

Investing activities include the purchase and sale of long-term assets such as land, buildings, plant and machinery etc. not held for resale. These activities also include the purchase and sale of such investments which are not included in cash equivalents. Cash flow from investing activities discloses the expenditures incurred for resources intended to generate future income and cash flows.

Examples of cash flows arising from investing activities are :

(*a*) Cash payments to acquire fixed assets (including intangibles);

(*b*) Cash receipts from sale of fixed assets (including intangibles);

(*c*) Cash payments to acquire shares, warrants or debt instruments of other enterprises (other than payments for those instruments considered to be cash equivalents);

(*d*) Cash receipts from sale of shares, warrants or debt instruments of other enterprises (other than receipts for those instruments considered to be cash equivalents).

(*e*) Cash advances and loans made to third parties;

(*f*) Cash receipts from the repayment of advances and loans made to third parties.

(*g*) Cash receipts of insurance claim for property involved in accident; and

(*h*) Cash receipts of interest and dividend.

(3) Cash Flows from Financing Activities :

Financing activities are the activities that result in change in capital and borrowings of the enterprise. Examples of cash flows arising from financing activities are :

(*a*) Cash receipts from issuing shares or other similar instruments;

(*b*) Cash receipts from short-term or long-term borrowings such as issuing debentures, bonds, loans (long-term as well as short term).

(*c*) Cash payment for Buy-back of Equity Shares;

(*d*) Cash repayments of short-term or long-term borrowings including redemption of debentures, bonds, preference shares, loans (short term or long term);

(*e*) Cash payments of interim dividend and previous year's proposed dividends both on Preference and Equity Shares;

(*f*) Cash payments for interest on long-term borrowings such as Debentures and interest on short-term borrowings such as Bank Overdraft and Cash Credit.

(*g*) Change in Bank Overdraft and Cash Credit.

(*h*) Payment of Preliminary Expenses (including share issue expenses).

Some Special Items :

AS–3 (Revised) has provided for the treatment of some special items as below :

(*i*) **Interest and Dividends** :— Cash inflow from interest and dividend and cash outflow on account of interest and dividend should be disclosed separately. Cash inflow arising from interest and dividends received should be shown as cash flow from investing activities whereas cash outflow on account of dividend paid on shares and interest paid on long term borrowings should be shown as cash flow from financing activity.

(*ii*) **Taxes on Income** :— Tax paid on income is a part of cash flows from operating activity. Hence, Taxes paid are shown as a deduction under 'cash flows from operating activities.'

Classification of Business Activities as per AS-3 showing 'Cash Inflows' and Cash Outflows'.

I. Operating Activities

Cash Inflows

(*i*) Cash Sales
(*ii*) Cash received from Royalty, Fees and Commission
(*iii*) Cash received from Debtors/Trade Receivables

Cash Outflows

(*i*) Cash Purchases
(*ii*) Cash paid to Creditors/Trade Payables
(*iii*) Payment of Operating Expenses like Wages, Salary, Office and Selling Expenses etc.
(*iv*) Payment of Income Tax

II. Investing Activities

Cash Inflows

(*i*) Proceeds from Sale of Fixed Assets
(*ii*) Proceeds from Sale of Non-Current Investments
(*iii*) Interest received on Debentures
(*iv*) Dividend received on Shares

Cash Outflows

(*i*) Purchase of Fixed Assets
(*ii*) Purchase of Non-Current Investments

I. Financing Activities

Cash Inflows

(*i*) Proceeds from Issue of Shares in Cash
(*ii*) Proceeds from Issue of Debentures in Cash
(*iii*) Loans raised (Long-term or Short-term)
(*iv*) Increase in Balance of Bank Overdraft or Cash Credit

Cash Outflows

(*i*) Payment for Buy-back of Equity Shares
(*ii*) Payment for Redemption of Preference Shares
(*iii*) Payment for Redemption of Debentures
(*iv*) Repayment of Loans (long-term or short-term)
(*v*) Payment of Interim Dividend and previous year's proposed Dividend
(*vi*) Payment of Interest on long term and short-term loans
(*vii*) Payment of Interest on Bank Overdraft/Cash Credit
(*viii*) Payment of Preliminary Exp. (including share issue exp.)
(*ix*) Decrease in Balance of Bank Overdraft or Cash Credit

Format of Cash Flow Statement

A cash flow statement may be prepared either by direct or indirect method. Format under indirect method is given below :

XYZ Ltd.

CASH FLOW STATEMENT *for the year ended* ....

(Indirect Method)

(as per Accounting Standard — 3 Revised)

		₹	₹
A. Cash Flows from Operating Activities :			
Net Profit before Tax (See Note No. 1)		....	
Adjustments for non cash and non operating items :			
Add : Depreciation	....		
Preliminary Expenses/Discount on issue of Debentures written off	....		
Goodwill, Patents and Trademarks Amortised	....		
Interest paid on short term and long term Borrowings	....		
Interest paid on Bank Overdraft/Cash Credit	....		
Loss on Sale of Fixed Assets	....		
Increase in Provision for Doubtful Debts	....	....	
Less : Interest Income	(..........)		
Dividend Income	(..........)		
Rental Income	(..........)		
Gain (Profit) on Sale of Fixed Assets	(..........)		
Decrease in Provision for Doubtful Debts	(..........)	(..........)	
Operating Profit before Working Capital Changes		....	
Add : Decrease in Current Assets	....		
Increase in Current Liabilities	....	....	
Less : Increase in Current Assets	(..........)		
Decrease in Current Liabilities	(..........)	(..........)	
Cash generated from operations		....	
Less : Income Tax paid (Net of Tax Refund received)		(..........)	
Net cash from (or used in) operating activities		....	....
B. Cash flows from Investing Activities :			
Proceeds from Sale of Tangible Fixed Assets		....	
Proceeds from Sale of Intangible Fixed Assets like goodwill		....	
Proceeds from Sale of Non-Current Investments		....	
Interest and Dividend Received		....	
Rent Received		....	
Purchase of Tangible Fixed Assets		(..........)	
Purchase of Intangible Fixed Assets like goodwill		(..........)	
Purchase of Non-Current Investments		(..........)	
Net cash from (or used in) Investing Activities		....	....

C. Cash flows from Financing Activities :		
Proceeds from issue of Shares and Debentures	....	
Proceeds from Other Long-term Borrowings	....	
Proceeds from Short-term Borrowings :		
(*i*) Increase in the Balance of Bank Overdraft or Cash Credit	....	
(*ii*) Decrease in the Balance of Bank Overdraft or Cash Credit	(..........)	
Payment of Interim Dividend	(..........)	
Payment of Proposed Dividend of Previous Year	(..........)	
Interest paid on Short-term and Long-term Borrowings	(..........)	
Interest Paid on Bank Overdraft/Cash Credit	(..........)	
Repayment of Loans (Whether short-term or long-term)	(..........)	
Redemption of Debentures/Preference Shares	(..........)	
Net cash from (or used in) financing activities	....	....
Net Increase (or Decrease) in Cash & Cash Equivalents (A+B+C)		....
Add : Cash and Cash Equivalents in the beginning of the year		....
Cash and Cash Equivalents at the end of the year		....

Note No. 1 : Calculation of Net Profit before Tax :

Particulars	
Net Profit of the current year (after appropriations)	....
Add : Transfer to Reserves (all transfers to Reserves from balances of the Statement of Profit & Loss)	....
Proposed Dividend of Previous year	....
Interim Dividend paid during the year	....
Provision for Tax made during the current year	....
Less : Refund of Tax	(..........)
Net Profit before Tax	....

Note : Amounts in brackets denote negative items, *i.e.* amounts that are to be deducted.

ISC Council's Instructions

(*i*) Short term Investments and Marketable Securities are to be taken as components of Cash and Cash Equivalents.

(*ii*) Current Investments will be considered as part of working capital changes.

(*iii*) Bank Overdraft and Cash Credit will be considered as financing activity as they are short-term borrowings.

IMPORTANT NOTE

Cash flow Statement only for Non-financing Companies is a part of syllabus.

Cash flow Statement for Financing Companies such as Bank and Mutual Fund Companies is excluded from syllabus.

ILLUSTRATION 1.

Classify the following into (*i*) Operating Activities, (*ii*) Investing Activities, (*iii*) Financing Activities and (*iv*) Cash Equivalents while preparing a Cash Flow Statement :

1. Cash Sales
2. Cash received from Trade Receivables
3. Purchase of Building
4. Sale of Building
5. Issue of Share Capital or Debentures
6. Buy-back of Equity Shares
7. Dividend paid
8. Interest paid on Debentures or Long-term Loans
9. Cash Purchases
10. Cash paid to trade payables
11. Redemption of Debentures and Preference Shares
12. Repayment of Long-term Loan
13. Office Expenses
14. Selling and Distribution Expenses
15. Manufacturing Expenses
16. Purchase of Goodwill
17. Sale of Patents
18. Purchase of Investments
19. Sale of Investments
20. Commission and Royalty received
21. Interest received on Investments
22. Dividend received on Shares
23. Rent paid
24. Rent received if (*a*) Company's main business is property business (*b*) Other
25. Income Tax Paid
26. Income Tax Refund received
27. Bank balance
28. Short-term Deposits in Bank
29. Investment in Short-term (or Marketable) Securities

SOLUTION :

Operating Activities : 1, 2, 9, 10, 13, 14, 15, 20, 23, 24 (*a*), 25, 26.

Investing Activities : 3, 4, 16, 17, 18, 19, 21, 22, 24 (*b*)

Financing Activities : 5, 6, 7, 8, 11, 12

Cash Equivalents : 27, 28, 29.

Points to Remember :

(1)

S. No.	*Item*	
(*i*)	Interest Received	Investing Activity
(*ii*)	Dividend Received	Investing Activity
(*iii*)	Interest Paid	Financing Activity
(*iv*)	Dividend Paid	Financing Activity

(2) For an Insurance Company, receipt of premium and payment of claim shall be classified as Operating Activities since they relate to main revenue producing activity for it.

(3) For a Real Estate Enterprise, purchase and sale of land and rent received shall be classified as Operating Activities since they relate to its main revenue producing activity.

(4) For a Computer manufacturing company, manufacturing and selling of Computers will be classified as Operating Activities since they relate to main revenue producing activity for it.

ILLUSTRATION 2.

Classify the following activities into (*i*) Operating Activities, (*ii*) Investing Activities, and (*iii*) Financing Activities :

1. Purchase of securities of a Company.
2. Brokerage paid for the purchase of securities.
3. Sale of securities of a Company.
4. Loans and advances made.
5. Receipts from the repayments of loans and advances.
6. Interest received on securities.
7. Dividend received on securities.
8. Interest paid on borrowings.
9. Dividend paid to shareholders.

SOLUTION :

All the transactions except No. 8 and 9, shall be classified as Investing Activities since they relate to acquisition and disposal of long-term assets. Transactions No. 8 and 9 (*i.e.*, interest paid and dividend paid) shall be classified as Financing Activity.

ILLUSTRATION 3.

Identify the following transactions as belonging to (*i*) Operating Activities, (*ii*) Investing Activities, (*iii*) Financing Activities and (*iv*) Cash and Cash Equivalents:

1. Cash Purchases of Goods.
2. Purchase of Shares.
3. Patents purchased.
4. Cash received against Services rendered.
5. Cash paid against Services taken.
6. Sale of building.
7. Income Tax paid on gain on sale of building.
8. Dividend paid.
9. Payment of Corporate Dividend Tax on Dividend paid.
10. Balance of Short-term Investments.
11. Balance of Marketable Securities.
12. Decrease in balance of Bank Overdraft or Cash Credit.
13. Interest paid on Bank Overdraft or Cash Credit.

SOLUTION :

Operating Activities : 1, 4, 5

Investing Activities : 2, 3, 6, 7
Financing Activities : 8, 9, 12, 13
Cash and Cash Equivalents : 10, 11

When does the Flow of Cash arise?

Cash flow arises when a transaction results in either increase or decrease in the amount of cash or cash equivalents.

(Cash and Cash equivalents include cash in hand, demand deposits with bank, Short-term Investments and marketable securities.)

ILLUSTRATION 4.

State which of the following would result in inflow/outflow of Cash or Cash Equivalents :

(*i*) Purchase of Inventory for cash.
(*ii*) Purchase of Goods on Credit.
(*iii*) Sale of Goods costing ₹10,000 for ₹12,000 for cash.
(*iv*) Sale of Goods on Credit.
(*v*) Purchase of a fixed asset by issue of shares.
(*vi*) Sale of a fixed asset (book value ₹15,000) at a loss of ₹5,000.
(*vii*) Cash received from trade receivables ₹9,000 and allowed discount ₹1,000.
(*viii*) Cash paid to trade Payables.
(*ix*) Shares issued for Cash.
(*x*) Issue of fully paid bonus shares.
(*xi*) Writing off bad debts against the provision for Doubtful Debts.
(*xii*) Dividend proposed by Directors.
(*xiii*) Declaration of interim dividend.
(*xiv*) Cash deposited into Bank.
(*xv*) Cash withdrawn from Bank. *(I.S.C. 2014)*
(*xvi*) Purchase of Marketable Securities for Cash.
(*xvii*) Sale of Marketable Securities for Cash at par.
(*xviii*) Charging depreciation on furniture. *(I.S.C. 2014)*

SOLUTION :

Statement showing the effect of transactions on Cash or Cash Equivalents.

Transaction	*Effect on Cash or Cash Equivalents*	*Reason*
(*i*)	Outflow	Cash is decreased by the amount of Inventory.
(*ii*)	No effect	Cash is not affected.
(*iii*)	Inflow	Cash is increased by ₹12,000.
(*iv*)	No effect	Cash is not affected as it is not a Cash transaction.
(*v*)	No effect	Cash is not affected as it is not a Cash transaction.
(*vi*)	Inflow	Cash is increased by ₹10,000.
(*vii*)	Inflow	Cash is increased by ₹9,000.

(viii)	Outflow	Cash is decreased
(ix)	Inflow	Cash is increased.
(x)	No effect	Cash is not affected. It is Capitalisation of profits.
(xi)	No effect	Cash is not affected as it is not a Cash transaction.
(xii)	No effect	Cash is not affected because proposed dividend will be paid in the next year, if approved by shareholders.
(xiii)	Outflow	Interim dividend declared is paid within 7 days of declaration.
(xiv)	No effect	Cash and Bank both are parts of Cash and Cash Equivalents.
(xv)	No effect	Cash and Bank both are parts of Cash and Cash Equivalents.
(xvi)	No effect	It is merely a conversion of cash into cash equivalents.
(xvii)	No effect	It is merely a conversion of cash equivalents into cash.
(xviii)	No effect	Cash is not affected.

ILLUSTRATION 5.

State which of the following would result in inflow, outflow or no flow of cash :

1. Issue of Debentures.
2. Issue of Debentures to the vendors for the purchase of Machinery.
3. Purchase of Own Debentures of ₹10,000 at 98%.
4. Redemption of Debentures.
5. Redemption of Debentures by converting them into equity shares.
6. Interest paid on Debentures.
7. Purchase of Patents.
8. Depreciation on Furniture.
9. Old Furniture Written off
10. Payment of Outstanding rent for previous month.
11. Deferred revenue expenditure charged to profit.
12. Declaration of Final Dividend.
13. Payment of Dividend.

SOLUTION :

Statement showing the effect of transactions on Cash or Cash Equivalents.

Transaction	*Effect on Cash or Cash Equivalents*	*Reason*
1.	Inflow	Cash is increased.
2.	No effect	Cash is not affected.
3.	Outflow	Cash is decreased by ₹9,800.
4.	Outflow	Cash is decreased.
5.	No effect	Cash is not affected.
6.	Outflow	Cash is decreased.
7.	Outflow	Cash is decreased.
8.	No effect	Cash is not affected.
9.	No effect	Cash is not affected.
10.	Outflow	Cash is decreased.

11.	No effect	Cash is not affected.
12.	Outflow	Cash is decreased as dividend will be paid immediately.
13.	Outflow	Cash is decreased.

Calculation of Cash Flow from Operating Activities

The term 'Operating activities' mean normal business transactions pertaining to purchase and sale of goods and services, Employee Benefit Expenses, Office Expenses etc. The basic information needed for the calculation of cash flow from operating activities is obtained from comparative balance sheets, statement of profit and loss of the current accounting period and the additional information. Figure of net profit disclosed by statement of profit and loss cannot be taken as cash flow from operating activities because there are some non-cash items in the statement of profit and loss. Such items do not result in the inflow or outflow of cash. As such, in order to ascertain the cash flow from operating activities, these non-cash items are eliminated from the net profit disclosed by statement of profit and loss. AS–3 (Revised) has stated two methods of ascertaining net cash flow from operating activities :

(*i*) Direct Method (this method is not in syllabus, hence it is not discussed)

(*ii*) Indirect Method

Indirect Method of Calculating Cash Flow from Operating Activities :

In this method we start with the net profit before Tax :

Step 1 :— Determination of Net Profit before Tax :

Net Profit before Tax is the starting point for the calculation of Cash Flow from Operating Activities. It is calculated as follows :

	₹
Difference between Opening Balance and Closing Balance of Statement of Profit & Loss	....
Add : Proposed Dividend (for previous year)	....
Interim Dividend paid during the year	....
Transfer to Reserves	....
Provision for Tax (for current year)	....
	....
Net Profit before Tax	....

It may be noted that 'Net Profit before Tax' must be calculated in 'Notes' below the Cash Flow Statement.

PROPOSED DIVIDEND

AS-4, Contingencies and Events Occurring After the Balance Sheet Date (Revised) prescribes that Proposed Dividend, both on Equity Shares and Preference Shares should not be shown as Short term Provision in the Balance Sheet but should be disclosed in 'Notes to Accounts' as Contingent Liability because it will be payable upon being declared (approved) by the shareholders in the Annual General Meeting. Annual General Meeting is held after the end of the financial year *i.e.*, in the next financial year.

The effect of this on Cash Flow Statement will be as follows :

(i) **Proposed Dividend for Previous Year** is shown as outflow of cash assuming it has been declared (approved) at the AGM in the Current year and has also been paid during the Current year.
It will also be added to Net Profit to determine the Net Profit before tax since it must have been appropriated (paid) from the net profit.

(ii) **Proposed Dividend for Current Year :** It is shown in Notes to Accounts as Contingent Liability. Hence, no effect is to be given to Proposed Dividend of the Current Year while preparing Cash Flow Statement.

Reasons for Addition or Deduction of various items for determining Net Profit before Tax :

(*i*) **Interim Dividend paid during the year** : It is paid during current year but it is an item of financing activity and not operating activity. Hence, it is added back to Net Profit to find out Cash generated from operating activities. It will be later shown as outflow under financing activity.

(*ii*) **Transfer to Reserves** : Transfer to General Reserve and Other Reserves is added back to Net Profit because it is an appropriation of profit and does not result in cash outflow.

(*iii*) **Provision for Tax for the Current Year** : Provision for Tax is added back to Net profit because creation of provision for tax does not result in outflow of Cash.

Step 2 :— Adjustment for Non-Cash and Non-Operating items :

(A) **Items to be added back to net profit** :— There are some items shown as expenses in the statement of profit and loss which do not result in the outflow of cash. Such items are called non-cash items. These items should be added back to net profit to calculate the cash profit. These items are generally as follows :—

(1) **Depreciation** :— Depreciation is shown as expenses in the statement of profit and loss. This reduces the profit made during the year without reducing the cash balance as it is a non-cash item. Hence, it is added back to profits in order to find out the operating profit.

(2) **Amortisation of Fictitious or Intangible Assets** :— When these assets are written off, these are shown as expenses or losses in the statement of profit & loss. But the writing off of these assets does not involve any cash payment. Hence they are added back to the profit for calculating the operating profit. These assets include the following :—

(I) Goodwill Written off;
(II) Preliminary Expenses Written off;
(III) Discount on issue of debentures Written off;
(IV) Trade Marks and Patent Rights Written off; and
(V) Bad Debts Written off.

(3) **Loss on Sale of Fixed Assets** :—Loss on sale of fixed assets is generally taken to the statement of profit and loss. It should be added back to profits so that operating profit can be ascertained. Net proceeds from the sale of fixed assets will be shown as inflow of cash from investing activities while preparing cash flow statement.

(4) **Interest on Long-term and Short-term Borrowings** :— Interest on long-term borrowings such as 'debenture interest' and interest on short-term

borrowings such as interest on Bank Overdraft and Cash Credit is added back to Net Profit because it is an expense relating to Financing Activity. It is shown as Outflow of Cash under Financing Activity.

(5) **Creation of Provisions :—** If any provision has been created out of profits such provision is added back to the profit earned during the year for calculating operating profit because such provision reduces the profits made during the year without reducing the cash balance of the firm. Such provisions may include the following :-

(I) Provision for Doubtful Debts;
(II) Provision for Discount on Trade Receivables;
(III) Provision for Expenses.

(B) **Items to be Deducted from Net Profits :—** There are some incomes which are shown in the statement of profit and loss, but they are non-operating incomes. These items should be deducted from net profits to find out the operating profit. These items are as follows :—

(1) **Profit on Sale of Fixed Assets :—** Total amount of cash received from sale of fixed assets is shown separately under Investing Activity in the cash flow statement as inflow of cash. Therefore profit on sale of fixed assets shown in statement of profit and loss must be deducted from the amount of profit.

(2) **Receipt of Interest and Dividend etc. :—** Receipt of interest and dividend from investments are receipts from non-operating activities. Hence, they are deducted from Net Profits and are shown as inflow of Cash under Investing Activities.

(3) **Rent Received :—** It is also a receipt from non-operating activities. Hence, it is also deducted from Net Profit and is shown as inflow of Cash under Investing Activities.

(4) **Re-transfer of Excess Provisions :—** When provisions for depreciation, doubtful debts etc. are made in excess of business needs, they are again transferred to the statement of profit & loss as incomes. They should also be deducted from profits because they do not affect the flow of cash in the current year in any way.

In addition to the above, the increase or decrease in current assets and current liabilities also influence the flow of cash from operating activities. Therefore, in Step 3, further adjustments in respect of increase or decrease in current assets and current liabilities except cash and cash equivalents are to be made to arrive at the cash flow from operating activities. This has been explained as below :—

Step 3 :— Adjustment in Respect of Changes in Current Assets and Current Liabilities :

Current assets and current liabilities go on changing frequently. Although these changes do not affect the amount of net profit, they affect the amount of cash generated from operating activities. Hence, in order to arrive at the figure of cash from operating activities, there is need for adjustments in respect of these changes. These adjustments will be made in the following manner :

(1) **Effect of Decrease in Current Assets such as Trade Receivables, Inventories, Prepaid Expenses, Accrued Incomes etc. :—** For example, Trade Receivables at the beginning of the year were ₹1,00,000 and trade receivables at the end of the year were ₹80,000. Decrease in trade receivables indicates that collections from trade receivables are more than the amount of credit sales during the year, hence

₹20,000 should be added to operating profit for arriving at the figure of net cash generated from operating activities.

The same treatment is made for the decrease in other current assets.

Thus, Decrease in current assets should be added to the figure of operating profit.

(2) **Effect of Increase in Current Assets such as Trade Receivables, Inventories, Prepaid Expenses, Accrued Incomes etc. :–** For example, trade receivables at the beginning of the year were ₹1,00,000 and trade receivables at the end of the year were ₹1,50,000. Increase in trade receivables indicates that collections from trade receivables are less than the amount of credit sales during the year, hence ₹50,000 should be deducted from operating profit for arriving at the figure of net cash generated from operating activities.

The same treatment is made for the increase in other current assets.

Thus, Increase in current assets should be deducted from the figure of operating profit.

(3) **Effect of Decrease in Current Liabilities such as Trade Payables, Outstanding Expenses, Incomes Received in Advance etc. :–** For example, trade payables at the beginning of the year were ₹60,000 and trade payables at the end of the year were ₹50,000. Decrease in trade payables indicates that payments to the trade payables were ₹10,000 more than the amount of credit purchases during the year. Hence, decrease in trade payables indicates that they are being paid more amount, which decreases the cash generated from operations. Therefore, the decrease in trade payables should be deducted from operating profit for arriving at the figure of net cash generated from operating activities.

The same treatment is made for the decrease in other current liabilities.

Thus, Decrease in current liabilities should be deducted from the figure of operating profit.

(4) **Effect of Increase in Current Liabilities such as Trade Payables, Outstanding Expenses, Incomes Received in Advance etc. :—** For example, trade payables at the beginning of the year were ₹60,000 and trade payables at the end of the year were ₹75,000. Increase in trade payables indicates that payments to trade payables were ₹15,000 less than the amount of credit purchases during the year. Hence, increase in trade payables indicates that they are being paid less amount, which increases the cash generated from operations. Therefore, the increase in trade payables should be added to operating profit for arriving at the figure of net cash generated from operating activities.

The same treatment is made for the increase in other current liabilities.

Thus, Increase in current liabilities should be added to the figure of operating profit.

After considering the net effect of increase or decrease in current assets and current liabilities cash from operating activities can be calculated with the help of the following formula :—

(+) Decrease in Trade Receivables	Current Assets
(+) Decrease in Inventories	
(+) Decrease in Prepaid Expenses	
(+) Decrease in Accrued Income	

Cash from Operating Activities = Operating Profit

(+) *Increase in Trade Payables*
(+) *Increase in Outstanding Expenses*
(+) *Increase in Unearned Income*
] Current Liabilities

(–) Increase in Trade Receivables
(–) Increase in Inventory
(–) Increase in Prepaid Expenses
(–) Increase in Accrued Income
] Current Assets

(–) *Decrease in Trade Payables*
(–) *Decrease in Outstanding Expenses*
(–) *Decrease in Unearned Income*
] Current Liabilities

It is clear from the above discussion that :—

Decrease in Current Assets increases the cash from operating activities.

Increase in Current Assets decreases the cash from operating activities.

Decrease in Current Liabilities decreases the cash from operating activities.

Increase in Current Liabilities increases the cash from operating activities.

As such,

Cash from Operating Activities = Operating Profit

(+) Decrease in Current Assets
(+) Increase in Current Liabilities
] These result in increase of cash, therefore, these should be added.

(–) Increase in Current Assets
(–) Decrease in Current Liabilities
] These result in decrease of cash, therefore, these should be deducted.

It should be remembered that the balance of cash and cash equivalents or changes in cash and cash equivalents from one period to another are not considered while calculating cash from operating activities.

Step 4 :— Deduct Income Tax Paid :

Income Tax paid is deducted from Cash Generated from Operating Activities.

The amount after above adjustments is Cash Flow from Operating Activities.

Distinction between Net Profit and Cash from Operations

S.No.	*Basis*	*Net Profit*	*Cash from Operations*
1.	**Meaning**	It indicates the net result of activities carried out during an accounting year.	It indicates the cash flow as a result of operating activities.

2.	**Non-Cash Operating Items**	It is calculated after taking into account the effect of non-cash operating items such as depreciation.	It is calculated after excluding the effect of non-cash operating items since these items represent merely the book entries.
3.	**Non-Operating Items**	It is calculated after taking into account the effect of non-operating items such as goodwill written off.	It is calculated after excluding the effect of non-operating items since these items do not relate to operating activities.
4.	**Basis of Calculation**	It is calculated on accrual basis.	It is calculated on cash basis.
5.	**Working Capital Changes**	For calculating net profit changes in working capital are not considered.	For calculating cash from operations changes in working capital are considered.

ILLUSTRATION 6.

Calculate 'Cash from Operating activities' from the following balances :

	March 31	
	2021	*2022*
Current Assets and Current Liabilities :	₹	₹
Debtors	80,000	60,000
Bills Receivable	7,000	10,000
Creditors	50,000	55,000
Bills Payable	8,000	6,000
Outstanding Expenses	1,000	1,500
Prepaid Expenses	1,800	1,600
Accrued Income	800	900
Income received in advance	700	—

Operating profit before working capital changes was ₹1,00,000.

SOLUTION : CASH FLOWS FROM OPERATING ACTIVITIES
for the year ended 31st March, 2022

	₹	₹
Operating profit before working capital changes		1,00,000
Add : Decrease in Current Assets :		
Debtors	20,000	
Prepaid Expenses	200	
Add : Increase in Current Liabilities :		
Creditors	5,000	
Outstanding Expenses	500	25,700
		1,25,700
Less : Increase in Current Assets :		
Bills Receivable	3,000	
Accrued Income	100	
Less : Decrease in Current Liabilities :		
Bills Payable	2,000	

Income received in Advance	700	5,800
Net Cash from Operating Activities		1,19,900

ILLUSTRATION 7.

X Ltd. made a profit of ₹5,00,000 after considering the following items :

		₹
I.	Goodwill Written off	5,000
II.	Depreciation on Fixed Tangible Assets	50,000
III.	Loss on sale of Fixed Tangible Assets (Machinery)	20,000
IV.	Provision for Doubtful Debts	10,000
V.	Gain on sale of Fixed Tangible Assets (Land)	7,500

Additional Information :

	31-3-2022 ₹	*31-3-2021* ₹
Trade Receivables	78,000	52,000
Prepaid Expenses	3,000	2,000
Trade Payables	51,000	40,000
Expenses Payable	20,000	34,000

You are required to Calculate Cash from Operating Activities.

SOLUTION :

X Ltd.

CALCULATION OF CASH FROM OPERATING ACTIVITIES

for the year ended 31st March, 2022

	₹	₹
Net Profit before Tax		5,00,000
Adjustments for non-cash and non-operating items :		
Add : Goodwill Written off	5,000	
Depreciation	50,000	
Loss on sale of Fixed Tangible Assets (Machinery)	20,000	
Provision for Doubtful Debts	10,000	85,000
		5,85,000
Less : Gain on Sale of Fixed Tangible Assets (Land)		7,500
Operating profit before working capital changes		5,77,500
Add : Increase in Current Liabilities :		
Trade Payables		11,000
		5,88,500
Less : Increase in Current Assets :		
Trade Receivables	(26,000)	
Prepaid Expenses	(1,000)	
Less : Decrease in Current Liabilities :		
Expenses Payable	(14,000)	(41,000)
Cash flow from Operating Activities		5,47,500

Note : (1) While calculating cash from operating activities, Provision for Doubtful debts is added back to Net Profit because creation of provision does not result in outflow of Cash.

ILLUSTRATION 8.

The net income of Blue Sky Ltd. for the year ended March 31, 2022 was ₹4,89,000. Depreciation charged for the year was ₹87,000. Income for the year was arrived at after adjusting for gain on sale of land ₹1,05,000, loss on sale of equipment ₹48,000 and writing off cost of equity issue ₹25,000.

Other Information :

	March 31, 2022 ₹	*March 31, 2021* ₹
Inventory	1,67,000	1,85,000
Receivables	1,45,000	1,42,000
Prepaid Expenses	8,000	12,000
Cash in Hand and at Bank	32,000	17,000
Payables	1,07,000	95,000
Expenses outstanding	9,000	13,000
Bank Overdraft	80,000	60,000

Required : Calculate cash from operating activities.

SOLUTION :

CALCULATION OF CASH FROM OPERATING ACTIVITIES

for the year ended 31st March, 2022

	₹	₹
Net Profit before Tax		4,89,000
Adjustments for non-cash and non-operating items :		
Add : Depreciation	87,000	
Loss on sale of equipment	48,000	
Cost of equity issue	25,000	1,60,000
		6,49,000
Less : Gain on sale of land		1,05,000
Operating profit before working capital changes		5,44,000
Add: Decrease in Current Assets :		
Inventory	18,000	
Prepaid Expenses	4,000	
Increase in Current Liabilities :		
Payables	12,000	34,000
		5,78,000
Less : Increase in Current Assets :		
Receivables	3,000	
Decrease in Current Liabilities :		
Expenses Outstanding	4,000	7,000
Net Cash Flow from Operating Activities		5,71,000

Working Notes :

(1) Cash in Hand and at Bank will not affect Cash from Operating Activities. It will be included in Cash and Cash Equivalents

(2) As per revised ISC Guidelines, Bank Overdraft and Cash Credit will be treated as 'Short-term Borrowings' and as per Para 17 of AS-3 (Revised) Cash proceeds from short term borrowings should be classified under Financing Activities. As such, Bank Overdraft and Cash Credit will be treated as 'Financing Activities' instead of Cash Equivalents.

PLEASE REMEMBER

While solving a question, **'Net Profit before Tax'** is written first of all. For calculating net profit before tax usually the following items are added to the net profit given in the question :

(*i*) Provision for Income Tax made during the year;

(*ii*) Proposed Dividend of Previous Year;

(*iii*) Interim Dividend paid to Shareholders;

(*iv*) Transfer to General Reserve or any other Reserve during the year.

It may be noted that 'Net Profit before Tax' must be calculated in 'Notes' below the Cash Flow Statement.

ILLUSTRATION 9.

The profit of Philips Ltd. after appropriations was ₹2,50,000. This profit was arrived at after taking into consideration the following items :

S.No.	*Particulars*	*Amount*
		₹
1.	Depreciation on Fixed Tangible Assets (Machinery)	20,000
2.	Loss on Sale of Fixed Tangible Assets (Furniture)	2,000
3.	Goodwill written off	9,000
4.	Provision for Taxation	35,000
5.	Transfer to General Reserve	17,500
6.	Gain on Sale of Fixed Tangible Assets (Machinery)	8,000

Additional information :

Particulars	*31.3.2021*	*31.3.2022*
	₹	₹
Trade Receivables (all good)	50,000	62,000
Trade Payables	45,000	55,000
Inventory	12,000	8,000
Income Received in Advance	8,000	----
Outstanding Expenses	6,000	3,000
Prepaid Expenses	----	5,000

You are required to calculate cash from operating activities.

SOLUTION :

CALCULATION OF CASH FLOW FROM OPERATING ACTIVITIES
for the year ended 31st March, 2022

Particulars		Amount
		₹
Net Profit before tax (Note 1)		3,02,500
Adjustments for non-cash and non-operating items :		
Add : Depreciation on Fixed Tangible Assets	20,000	
Loss on sale of Fixed Tangible Assets	2,000	
Goodwill written off	9,000	31,000
		3,33,500
Less : Gain on Sale of Machinery		(8,000)
Net Profit before Working Capital Changes		3,25,500
Add : Decrease in Current Assets :		
Inventory	4,000	
Increase in Current Liabilities :		
Trade Payables	10,000	14,000
		3,39,500
Less : Increase in Current Assets :		
Trade Receivables	(12,000)	
Prepaid Expenses	(5,000)	
Decrease in Current Liabilities :		
Outstanding Expenses	(3,000)	
Income Received in Advance	(8,000)	(28,000)
Cash Generated from Operating Activities		3,11,500
Less : Tax paid		(35,000)
Net Cash Flow from Operating Activities		2,76,500

Working Note :

(1) Calculation of Net Profit before Tax :

Particulars	Amount
	₹
Net profit after appropriations	2,50,000
Add : Provision for Tax	35,000
Add : Transfer to General Reserve	17,500
Net Profit before Tax	3,02,500

(2) It will be assumed that provision for taxation made during the year equals the payment of taxation during the year.

ILLUSTRATION 10.

Charles Ltd. made a profit of ₹1,00,000 after charging Depreciation of ₹20,000 on assets and a transfer to General Reserve of ₹30,000. The goodwill written off was ₹7,000 and the gain on sale of Machinery was ₹3,000. The other information available to you (changes in the value of Current Assets and Current Liabilities) is as follows :

At the end of the year Trade Receivables showed an increase of ₹6,000; Trade Payables an increase of ₹10,000; Prepaid Expenses an increase of ₹200 and Outstanding Expenses a Decrease of ₹2,000. Ascertain the cash flow from the operating activities. *(NCERT Modified)*

SOLUTION :

CALCULATION OF CASH FROM OPERATING ACTIVITIES

for the year ended ....

	₹	₹
Net Profit before Tax (Note 1)		1,30,000
Adjustments for non-cash and non-operating items :		
Add : Depreciation	20,000	
Goodwill written off	7,000	27,000
		1,57,000
Less : Gain on sale of Machinery		3,000
Operating profit before working capital changes		1,54,000
Add : Increase in Current Liabilities :		
Trade Payables		10,000
		1,64,000
Less : Increase in Current Assets :		
Trade Receivables	6,000	
Prepaid Expenses	200	
Decrease in Current Liabilities :		
Outstanding Expenses	2,000	8,200
Net Cash Flow from Operating Activities		1,55,800

Note : (1) Calculation of Net Profit before tax :

Profit made during the year	1,00,000
Add : Transfer to General Reserve	30,000
Net Profit before Tax	1,30,000

ILLUSTRATION 11.

From the following figures calculate cash from operating activities :

	31.3.2021 ₹	31.3.2022 ₹
Balance of Profit & Loss	3,00,000	2,50,000
Provision for Depreciation	60,000	80,000
Outstanding Wages	18,000	15,000
Prepaid Insurance	6,000	9,000
Goodwill	40,000	32,000
Provision for Doubtful Debts	10,000	14,000
Balance of Trade Receivables	1,40,000	98,000
Cash and Bank Balance	30,000	25,000

SOLUTION : CALCULATION OF CASH FROM OPERATING ACTIVITIES

for the year ended 31st March, 2022

	₹	₹
Net Loss (Note 1)		(50,000)
Adjustments for non-cash and non-operating items :		
Add : Depreciation (₹80,000 – ₹60,000)	20,000	
Goodwill written off (₹40,000 – ₹32,000)	8,000	
Transfer to Provision for Doubtful Debts (₹10,000 – ₹14,000)	4,000	32,000
Operating loss before working capital changes		(18,000)
Add : Decrease in Current Assets :		
Trade Receivables		42,000
		24,000
Less : Increase in Current Assets :		
Prepaid Insurance	3,000	
Less : Decrease in Current Liabilities :		
Outstanding Wages	3,000	(6,000)
Net Cash Flow from Operating Activities		18,000

Notes : (1) Calculation of Net Loss :

Balance of Profit & Loss on 31.3.2022	2,50,000
(–) Balance of Profit & Loss on 31.3.2021	3,00,000
Net Loss during the year	(50,000)

(2) Cash and Bank Balance will not affect Cash flow from operating activities. It will be included in Cash & Cash Equivalents.

ILLUSTRATION 12.

The profit of Jova Ltd. for the year ended 31st March, 2019 after appropriations was ₹2,50,000.

Additional Information :

S. No.	*Particulars*	*Amount*
		₹
1.	Depreciation of Machinery	20,000
2.	Goodwill written off	9,000
3.	Loss on Sale of Furniture	2,000
4.	Transfer to General Reserve	22,500

The following was the position of its Current Assets and Current Liabilities as at 31st March, 2018 and 2019 :

Particulars	*31.3.2018*	*31.3.2019*
	₹	₹
Income Received in Advance	8,000	—
Inventory	12,000	8,000

Calculate the Cash Flow from Operating Activities.

(C.B.S.E. 2020, Chennai, Mumbai)

SOLUTION :

Jova Ltd.
CASH FLOW FROM OPERATING ACTIVITIES
for the year ended 31st March, 2019

Particulars	*Amount*
	₹
Net Profit before Tax(1)	2,72,500
Adjustment for Non Cash and Non Operating Items	
Add : Depreciation	20,000
,, Goodwill Written Off	9,000
,, Loss on Sale of Furniture	2,000
Operating Profit before Working Capital Changes	3,03,500
Add : Decrease in Inventory	4,000
	3,07,500
Less : Decrease in Advance Income	(8,000)
Net Cash Flow from Operating Activities	2,99,500

Working Note : (1)

Calculation of Net Profit before Tax

	₹
Net Profit	2,50,000
Add : Transfer to General Reserve	22,500
	2,72,500

ILLUSTRATION 13.

Calculate Cash Flow from Operating Activities from the following :

	31st March 2020 (₹)	*31st March 2021 (₹)*
Surplus *i.e.*, Balance in Statement of Profit and Loss	(40,000)	(50,000)
Plant & Machinery	4,00,000	3,60,000
8% Debentures	5,00,000	6,00,000
Trade Receivables	4,00,000	3,50,000
Trade Payables	1,80,000	2,20,000
Provision for Doubtful Debts	20,000	18,000
10% Non Current Investments	2,00,000	2,50,000
Goodwill	30,000	45,000
Inventories	3,60,000	5,10,000
Short Term Loans	40,000	45,000

Additional Information :

(*i*) New Debentures have been issued on 1st Oct. 2020.

(*ii*) New Investments have been made at the end of the current year.

SOLUTION :

CASH FLOW FROM OPERATING ACTIVITIES

for the year ended 31st March, 2021

	₹	₹
Net Loss for the year (Note 1)		(10,000)
Adjustments for the Non-Cash and Non-Operating items :		
Add : Depreciation on Plant & Machinery		
(₹4,00,000 – ₹3,60,000)	40,000	
Interest on Debentures	44,000	84,000
		74,000
Less : Decrease in Provision for Doubtful Debts	2,000	
Interest on Investments	20,000	(22,000)
Operating Profit before Working Capital Changes		52,000
Add : Decrease in Current Assets :		
Trade Receivables	50,000	
Increase in Current Liabilities :		
Trade Payables	40,000	90,000
		1,42,000
Less : Increase in Current Assets :		
Inventories		(1,50,000)
Cash used (or lost) in Operating Activities		(8,000)

Notes :

(1) Calculation of Net Profit (Loss) during the year :

	₹
Net Loss as at 31st March, 2020	(40,000)
Net Loss as at 31st March, 2021	(50,000)
Net Loss during the year 2020-21	(10,000)

Net Loss of (₹50,000) as at 31st March 2021 includes net loss of (₹40,000) as at 31st March 2020 also.

(2) ₹15,000 has been paid for the purchase of a fixed asset, *i.e.*, Goodwill. It will not be shown in the above statement because the purchase of a fixed asset does not affect cash from operating activities. It will be shown as Outflow of Cash while calculating Cash Flow from Investing Activities.

(3) Short term loans will be taken to Financing Activities as a source of Funds.

ILLUSTRATION 14.

From the following balance sheets of ABC Ltd., find out cash from operating activities only :

Particulars	*Note No.*	*31-3-2022* ₹	*31-3-2021* ₹
I. EQUITY AND LIABILITIES :			
(1) **Shareholder's Funds :**			
(a) Share Capital		35,000	30,000
(b) Reserve and Surplus	1	22,000	3,500

(2) Non-Current Liabilities			
Long-term Borrowings	2	25,000	21,000
(3) Current Liabilities			
Trade Payables		12,500	8,500
TOTAL		94,500	63,000
II. ASSETS :			
(1) Non-Current Assets :			
(*a*) Fixed Assets			
(*i*) Tangible Assets	3	41,000	32,000
(*ii*) Intangible Assets	4	8,000	10,000
(*b*) Non Current Investments	5	8,000	3,000
(2) Current Assets :			
(*a*) Inventory		24,500	6,000
(*b*) Cash & Bank Balance		13,000	12,000
TOTAL		94,500	63,000

Notes :		*2022*	*2021*
(1)	Reserve & Surplus :		
	General Reserve	15,000	9,500
	Profit & Loss Balance	7,000	(6,000)*
		22,000	3,500
	* Bracket denotes negative balance.		
(2)	Long-term Borrowings :		
	10% Debentures	25,000	21,000
(3)	Tangible Assets :		
	Machinery	54,000	41,000
	Less : Provision for Depreciation	13,000	9,000
		41,000	32,000
(4)	Intangible Assets :		
	Goodwill	8,000	10,000

(5) Rate of interest on Investments is 10% p.a.

Additional Information :

Debentures were issued on 31.3.2022.

Investments were made on 31.3.2022.

SOLUTION :

CALCULATION OF CASH FROM OPERATING ACTIVITIES

(for the year ended 31st March, 2022)

	₹	₹
Net Profit before Tax (Note 1)		18,500
Adjustments for non-cash and non-operating items :		
Add : Payment of Interest on Long-term Borrowings (Debentures) (10% on ₹21,000)	2,100	

Depreciation (₹13,000 – ₹9,000)	4,000	
Goodwill written off	2,000	8,100
		26,600
Less : Interest on Non-Current Investments		300
Operating profit before working capital changes		26,300
Add : Increase in Current Liabilities :		
Trade Payables		4,000
		30,300
Less : Increase in Current Assets :		
Inventory		(18,500)
Net Cash flow from Operating Activities		11,800

Notes : (1) Calculation of Net Profit before Tax :

	₹
Net Profit during Current year (₹7,000 + ₹6,000)	13,000
Add : Transfer to General Reserve	5,500
	18,500

Negative balance of Profit & Loss amounting to ₹6,000 appearing in the balance sheet on 31.3.2021 represents an amount of loss. In the current year, after covering this loss of ₹6,000 the Profit & Loss shows a profit of ₹7,000. It means that net profit during the current year must have been ₹7,000 + ₹6,000 = ₹13,000.

ILLUSTRATION 15.

From the following summarised Balance Sheets of a company, calculate the Cash Flow from operating activities :

Particulars	*Note No.*	*31-3-2019* ₹	*31-3-2018* ₹
I. EQUITY AND LIABILITIES :			
(1) Shareholder's Funds :			
(*a*) Share Capital		50,000	50,000
(*b*) Reserve and Surplus		60,000	30,000
(2) Non-Current Liabilities			
Long-term Borrowings	1	80,000	60,000
(3) Current Liabilities			
(*a*) Trade Payables		35,000	48,000
(*b*) Short term Provision	2	40,000	32,000
TOTAL		2,65,000	2,20,000
II. ASSETS :			
(1) Non-Current Assets :			
(*a*) Fixed Assets		1,40,000	1,00,000
(*b*) Investments		30,000	40,000
(2) Current Assets :			
(*a*) Inventory		45,000	30,000
(*b*) Trade Receivables		40,000	30,000
(*c*) Cash & Bank Balance		10,000	20,000
TOTAL		2,65,000	2,20,000

	31.3.2019	31.3.2018
Notes : (1) Long-term Borrowings :		
6% Debentures	80,000	60,000
(2) Short term Provision :		
Provision for Tax	40,000	32,000

SOLUTION : CASH FLOWS FROM OPERATING ACTIVITIES

for the year ended 31st March, 2019

	₹	₹
Net Profit before Tax (Note 1)		70,000
Adjustments for non-cash and non-operating items :		
Add : Interest on Debentures$^{(2)}$		3,600
Operating profit before working capital changes		73,600
Less : Decrease in Current Liabilities :		
Trade Payables	13,000	
Increase in Current Assets :		
Inventory	15,000	
Trade Receivables	10,000	38,000
		35,600
Payment of Tax (for 2018)		(32,000)
Net Cash Flow from Operating Activities		3,600

Notes : (1) Calculation of Net Profit before Tax :	₹
Balance of Reserve and Surplus on 31st March, 2019	60,000
(–) Balance of Reserve and Surplus on 31st March, 2018	30,000
	30,000
Add : Provision for Tax made during the year	40,000
	70,000

(2) It has been assumed that new debentures have been issued on 31st March, 2019. As such, interest on Debentures = ₹60,000 × $\frac{6}{100}$ = ₹3,600.

ILLUSTRATION 16.

The following is the Statement of Profit and Loss of Yamuna Limited for the year ended March 31, 2022 :

Particulars	*Note No.*	*Amount*
		₹
I. Revenue from Operations (Sales)		10,00,000
II. Expenses :		
Purchases		5,00,000
Changes in Inventories (Opening Inventory − Closing Inventory) (2,50,000 − 2,00,000)		50,000
Other Expenses		3,00,000
Total Expenses		8,50,000
III. Profit before Tax (I − II)		1,50,000

Additional Information :

(*i*) Trade receivables decrease by ₹30,000 during the year.
(*ii*) Prepaid expenses increase by ₹5,000 during the year.
(*iii*) Trade payables decrease by ₹15,000 during the year.
(*iv*) Outstanding expenses increased by ₹3,000 during the year.
(*v*) Operating expenses included depreciation of ₹25,000.

Compute net cash provided by operations for the year ended March 31, 2022 by the indirect method.

SOLUTION : CASH FLOWS FROM OPERATING ACTIVITIES
for the year ended 31st March, 2022

	₹	₹
Net Profit before Tax		1,50,000
Adjustments for non-cash and non-operating items :		
Add : Depreciation		25,000
Operating profit before working capital changes		1,75,000
Add : Decrease in Current Assets :		
Inventory	50,000	
Trade Receivables	30,000	
Increase in Current Liabilities :		
Outstanding Expenses	3,000	83,000
		2,58,000
Less : Increase in Current Assets :		
Prepaid expenses	5,000	
Decrease in Current Liabilities :		
Trade Payables	15,000	20,000
Net Cash from Operating Activities		2,38,000

ILLUSTRATION 17.

From the following information, calculate cash from operating activities :

	₹
Profit and Loss Balance on 1st April, 2021	25,000
Profit and Loss Balance on 31st March, 2022	80,000
Depreciation on Fixed Assets	12,500
Amortisation of Goodwill	8,000
Loss on Sale of Machine	20,000
Provision for Taxation	15,000
Transfer to General Reserve	30,000
Decrease in Trade Receivables	22,800
Decrease in Trade Payables	4,700
Outstanding Expenses on 1st April, 2021	5,000
Outstanding Expenses on 31st March, 2022	6,500
Prepaid Expenses on 1st April, 2021	2,000

SOLUTION : CALCULATION OF CASH FROM OPERATING ACTIVITIES

for the year ended 31st March, 2022

	₹	₹
Net Profit before Tax (Note 1)		1,00,000
Adjustments for non-cash and non-operating items :		
Add : Depreciation	12,500	
Goodwill	8,000	
Loss on Sale of Machine	20,000	40,500
		1,40,500
Add : Decrease in Current Assets :		
Decrease in Trade Receivables	22,800	
Decrease in Prepaid Expenses	2,000	
Add : Increase in Current Liabilities :		
Increase in Outstanding Expenses	1,500	26,300
		1,66,800
Less : Decrease in Current Liabilities :		
Decrease in Trade Payables		4,700
Cash generated from operating activities		1,62,100
Tax paid(2)		15,000
Net Cash Flow from Operating Activities		1,47,100

Notes : (1) Calculation of Net Profit before Tax :

	₹
Profit and Loss Balance on 31st March, 2022	80,000
Less : Profit and Loss Balance on 31st March, 2021	25,000
	55,000
Add : Transfer to General Reserve	30,000
Provision for Tax made during the current year	15,000
Net Profit before Tax	1,00,000

(2) It is assumed that tax paid during the year is equivalent to provision for taxation made during the year.

Cash Flows from Investing Activities

Investing activities of an enterprise refer to acquisition (purchase) and disposal (sale) of Long term Assets and Other Investments which are not included in Cash equivalents.

CALCULATION OF NET CASH FROM INVESTING ACTIVITIES

Particulars	₹
Proceeds from Sale of Fixed Assets	....
Payment for Purchase of Fixed Assets	(..........)*
Proceeds from Sale of Non-Current Investments	....
Payment for Purchase of Non-Current Investments	(..........)
Interest Received on Debentures	....
Dividend Received on Shares	....
Net Cash Inflow/Used from Investing Activities	....

*Bracket denotes minus items.

ILLUSTRATION 18.

From the following particulars, calculate cash flows from investing activities :

	Purchased ₹	*Sold* ₹
Plant	6,20,000	2,00,000
Investments	2,40,000	80,000
Goodwill	1,00,000	—
Patents		1,50,000

Interest received on debentures held as investment ₹8,000.
Interest paid on debentures issued ₹15,000.
Dividend received on shares held as investment ₹20,000.
Dividend paid on equity share capital ₹25,000.

A plot of land was purchased out of the surplus funds for investment purposes and was let out for commercial use and rent received ₹30,000.

SOLUTION : CASH FLOWS FROM INVESTING ACTIVITIES

	₹
Purchase of Plant	(6,20,000)
Proceeds from sale of Plant	2,00,000
Purchase of Investments	(2,40,000)
Proceeds from sale of Investments	80,000
Purchase of Goodwill	(1,00,000)
Proceeds from sale of Patents	1,50,000
Interest received	8,000
Dividend received	20,000
Rent received	30,000
Net cash used in Investing Activities	(4,72,000)

Working Note : Interest paid ₹15,000 and dividend paid ₹25,000 will not be recorded in cash flows from investing activities. They will be recorded in cash flows from financing activities.

Ascertaining Missing Figure by Preparing Fixed Asset Account

Case I :— Preparation of Fixed Asset Account on Written Down Value Basis :

If the balance sheet does not contain the item of 'Provision for Depreciation' or 'Accumulated Depreciation' for both the years, it means that the fixed assets shown in the balance sheet are shown at their written down value and hence fixed assets account will be prepared on written down value basis. In such cases, it should be noted that if the amount of current year's depreciation is given in adjustments, it should be shown on the credit side of asset account.

The balance of asset account will now show purchase or sale of asset. If the credit side is in excess of the debit side, the amount of difference will be treated as purchase of asset and if the debit side is in excess, the amount of difference will be treated as sale of asset.

Loss or Profit on Sale of Fixed Assets : If there is a loss on sale of fixed asset, it is put to the credit side of the asset account and if there is a profit on sale of fixed asset, it is put to the debit side of the asset account.

ILLUSTRATION 19.

Calculate Cash Flow from Investing Activities from the following particulars :

	1st April, 2021	*31st March, 2022*
	₹	₹
Plant & Machinery (Written Down value)	7,20,000	8,60,000

Information :

(*i*) Depreciation charged during the year ₹85,000.

(*ii*) Plant & Machinery having a written down value of ₹1,10,000 was sold for ₹1,25,000.

SOLUTION :

Dr. PLANT AND MACHINERY ACCOUNT Cr.

Particulars	₹	*Particulars*	₹
To Balance b/d	7,20,000	By Bank A/c (Sale Proceeds)	1,25,000
To Gain on Sale	15,000	By Depreciation A/c	85,000
To Bank A/c (Balancing Figure, being purchase)	3,35,000	By Balance c/d	8,60,000
	10,70,000		10,70,000

CASH FLOW FROM INVESTING ACTIVITIES

Particulars	₹
Proceeds from sale of Plant & Machinery	1,25,000
Payment for purchase of Plant & Machinery	(3,35,000)
Net Cash used in Investing Activities	(2,10,000)

ILLUSTRATION 20.

Calculate net cash flows from investing activities from the following information:

	31-3-2021	*31-3-2022*
	₹	₹
Building (Written Down Value)	6,00,000	7,50,000

Additional Information :

(*i*) Building costing ₹1,00,000 on which ₹30,000 had accumulated as depreciation was sold for ₹60,000.

(*ii*) Depreciation charged on building for the year ended 31-3-2022 ₹50,000.

SOLUTION :

Dr. BUILDING ACCOUNT Cr.

Particulars	₹	*Particulars*	₹
To Balance b/d	6,00,000	By Bank A/c	60,000

To Bank A/c (Balancing figure, being purchase)	2,70,000	By Loss on Sale A/c (₹1,00,000 – ₹30,000 – ₹60,000) By Depreciation A/c By Balance c/d	10,000 50,000 7,50,000
	8,70,000		8,70,000

Net Cash Flows from Investing Activities :

	₹
Sale of Building	60,000
Purchase of Building	(2,70,000)
Net Cash used in Investing Activities	(2,10,000)

ILLUSTRATION 21.

Calculate Cash Flows from Investing Activities from the following information :

Particulars	*31st March 2015*	*31st March 2014*
	₹	₹
Investment in shares of Miko Ltd.	18,00,000	8,00,000
12% Long Term Investments	1,50,000	5,00,000
Plant and Machinery	6,00,000	4,00,000
Goodwill	1,20,000	40,000

Additional information :

(*i*) 9% dividend was received from Miko Ltd.

(*ii*) A machine costing ₹50,000 (depreciation provided thereon ₹15,000) was sold for ₹40,000. Depreciation charged during the year was ₹55,000.

(C.B.S.E. 2017, Comptt. Outside Delhi)

SOLUTION : CASH FLOWS FROM INVESTING ACTIVITIES

Particulars	*Amount*
	₹
Sale of Plant and Machinery	40,000
Purchase of Plant and Machinery	(2,90,000)
Investment in Shares of Miko Ltd.	(10,00,000)
Dividend received from Miko Ltd. (Note 1) (9% on ₹8,00,000)	72,000
Sale of Long Term Investments	3,50,000
Interest received on Investments (Note 1) (12% on ₹5,00,000)	60,000
Goodwill Purchased	(80,000)
Net Cash used in Investing Activities	(8,48,000)

Note 1 :

It is assumed that Investment in Shares of Miko Ltd. were made and Long Term Investments were sold on 31st March 2015.

In case it is assumed that Investment in Shares of Miko Ltd. were made and Investments were sold on 1st April, 2014, dividend would be ₹1,62,000 and interest would be ₹18,000 and Cash Flows from Investing Activities would be ₹8,00,000

Dr. PLANT AND MACHINERY A/C (On Written Down Value Basis) Cr.

Particulars	Amount	Particulars	Amount
	₹		₹
To Balance b/d	4,00,000	By Bank A/c	40,000
To Gain on Sale	5,000	By Depreciation A/c	55,000
To Bank A/c (Purchase of Machinery)	2,90,000	By Balance c/d	6,00,000
	6,95,000		6,95,000

ILLUSTRATION 22

From the following information calculate the amount of Cash Flows from Investing Activities :

Particulars	31.03.2021	31.03.2022
	₹	₹
Plant and Machinery	8,50,000	10,00,000
Non Current Investments	40,000	1,00,000
Land (At cost)	2,00,000	1,00,000

Additional Information

(*i*) Depreciation charged on Plant and Machinery was ₹50,000.

(*ii*) Plant and Machinery with a book value of ₹60,000 was sold for ₹40,000.

(*iii*) Land was sold at a gain of ₹60,000.

SOLUTION CALCULATION OF CASH FROM INVESTING ACTIVITIES

Particulars	Amount
	₹
Sale of Plant and Machinery	40,000
Sale of Land (See Note 1)	1,60,000
Purchase of Plant & Machinery (See Note 2)	(2,60,000)
Purchase of Non-Current Investments	(60,000)
Net Cash flows from Investing Activities	(1,20,000)

Working Note No. 1

Dr. LAND A/C Cr.

Particulars	₹	Particulars	₹
To Balance b/d	2,00,000	By Bank (Sale of Land) (Balancing Figure)	1,60,000
To Gain on Sale of Land	60,000	By Balance c/d	1,00,000
	2,60,000		2,60,000

Working Note No. 2

Dr. PLANT & MACHINERY A/C (On Written Down Value Basis) Cr.

Particulars	₹	Particulars	₹
To Balance b/d	8,50,000	By Depreciation	50,000
To Bank		By Bank (Sale of Machinery)	40,000
(Purchase of Machinery)		By Loss on Sale of Machinery	20,000
(Balancing Figure)	2,60,000	By Balance c/d	10,00,000
	11,10,000		11,10,000

Case II :— Preparation of Fixed Asset Account on Original Cost Basis :

If the balance sheet contains an item of 'Provision for Depreciation' or 'Accumulated Depreciation' for both the years, it means that the fixed assets shown in the balance sheet are shown at their original cost. In such cases, fixed assets account and provision for depreciation account should be prepared separately. By preparing 'fixed assets account' the amount of fixed assets purchased or sold during the year will be found out and by preparing 'provision for depreciation account' the amount of depreciation charged during the year will be found out.

ILLUSTRATION 23.

The balances in Machinery account and Accumulated depreciation account as on March 31, 2018 and 2019 are given below :

Balance as at	*March 31, 2018*	*March 31, 2019*
	₹	₹
Machinery	5,00,000	6,00,000
Accumulated depreciation	1,64,000	1,80,000

During the year, a Machine costing ₹1,00,000 accumulated depreciation thereon ₹44,000 was sold for ₹30,000.

Required :

(*i*) Compute the amount of machinery purchased, depreciation charged for the year and loss on sale of machinery.

(*ii*) How each of the item related to the machinery will be reported in the statement of cash flows?

SOLUTION :

(*i*) Calculation of machinery purchased :

MACHINERY ACCOUNT (On Original Cost Basis)

	₹		₹
To Balance b/d	5,00,000	By Bank A/c (Sale proceeds)	30,000
To Bank A/c (balancing figure, being purchase of machinery)	2,00,000	By Accumulated Depreciation A/c (Dep. on machinery sold)	44,000
		By Loss on sale (₹1,00,000 – ₹44,000	

		– ₹30,000)	26,000
		By Balance c/d	6,00,000
	7,00,000		7,00,000

Calculation of Current year's depreciation :

ACCUMULATED DEPRECIATION ACCOUNT

	₹		₹
To Machinery A/c (transfer of depreciation on sold machinery)	44,000	By Balance b/d	1,64,000
To Balance c/d	1,80,000	By Depreciation A/c (balancing figure, being current year's depreciation)	60,000
	2,24,000		2,24,000

(*ii*) CASH FLOW STATEMENT

for the year ending 31st March, 2019

Particulars	₹
Cash Flows from Operating Activities :	
Net Profit	—
Add : Depreciation charged on Machinery	60,000
Loss on sale of Machinery	26,000
Cash Flows from Investing Activities :	
Sale of Machinery	30,000
Purchase of Machinery	(2,00,000)
Cash Flows from Financing Activities :	—

ILLUSTRATION 24.

From the following particulars, calculate Cash from Investing Activities :

Particulars	*Opening Balances*	*Closing Balances*
	₹	₹
Plant & Machinery (at cost)	3,00,000	3,20,000
Accumulated Depreciation	90,000	1,00,000
Patents	2,60,000	1,40,000
Goodwill	80,000	1,00,000

Additional Information :

During the year :

(*i*) Depreciation charged on Plant and Machinery ₹36,000.

(*ii*) A machine having a book value of ₹20,000 was sold for ₹16,000.

(*iii*) Patents having a book value of ₹80,000 was sold for ₹1,10,000.

(I.S.C. Specimen Question Paper, 2018)

SOLUTION: CASH FLOW FROM INVESTING ACTIVITIES

Particulars	₹
Sale of Machinery	16,000
Purchase of Machinery	(66,000)
Sale of Patents	1,10,000
Purchase of Goodwill	(20,000)
Net Cash Flow from Investing Activities	40,000

Working Notes :

(1)

Dr. ACCUMULATED DEPRECIATION ACCOUNT Cr.

Particulars	₹	*Particulars*	₹
To Plant & Machinery A/c (Balancing figure, being the accumulated depreciation on machinery sold)	26,000	By Balance b/d	90,000
To Balance c/d	1,00,000	By Depreciation A/c	36,000
	1,26,000		1,26,000

(2) Balancing figure of Accumulated Depreciation A/c ₹26,000 represents the accumulated depreciation on machinery sold. It is transferred to the Cr. side of Plant & Machinery A/c.

(3)

Dr. PLANT & MACHINERY ACCOUNT Cr.

Particulars	₹	*Particulars*	₹
To Balance b/d	3,00,000	By Bank A/c (Sale)	16,000
To Bank A/c (Balancing figure, being purchase)	66,000	By Accumulated Dep. A/c (being accumulated depreciation on machinery sold)	26,000
		By Loss on Sale of Machinery (₹20,000 – ₹16,000)	4,000
		By Balance c/d	3,20,000
	3,66,000		3,66,000

(4)

Dr. PATENTS ACCOUNT Cr.

Particulars	₹	*Particulars*	₹
To Balance b/d	2,60,000	By Bank A/c (Sale)	1,10,000
To Profit on Sale	30,000	By Statement of P & L (Balancing figure, being patents written off)	40,000
		By Balance c/d	1,40,000
	2,90,000		2,90,000

ILLUSTRATION 25.

The following balances appeared in the Plant & Machinery Account and Accumulated Depreciation Account in the books of Piyush Ltd :

Balances as at	*31.3.2014*	*31.3.2013*
	₹	₹
Plant & Machinery	9,32,000	8,50,000
Less : Accumulated Depreciation	(4,40,000)	(4,32,000)

During the year 2013-14, the company provided depreciation amounting to ₹80,000 and a machine costing ₹1,05,000 was sold at a profit of 20% on its book value.

You are required to calculate Cash from Investing Activities.

(ISC Sample Question Paper, 2015)

SOLUTION : CASH FLOW FROM INVESTING ACTIVITIES

Particulars	₹
Proceeds from Sale of Plant & Machinery	39,600
Purchase of Plant & Machinery	(1,87,000)
Net Cash used in Investing Activities	(1,47,400)

Working Notes :

(1)

Dr. ACCUMULATED DEPRECIATION ACCOUNT Cr.

Particulars	₹	*Particulars*	₹
To Plant & Machinery A/c (Balancing figure, being the accumulated depreciation on machinery sold)	72,000	By Balance b/d	4,32,000
To Balance c/d	4,40,000	By Depreciation A/c	80,000
	5,12,000		5,12,000

(2) Balancing figure of Accumulated Depreciation A/c ₹72,000 represents the accumulated depreciation on machinery sold. It is transferred to the Cr. side of Plant & Machinery A/c.

(3)

	₹
Original Cost of Machinery sold	1,05,000
Less : Accumulated Depreciation on Machinery sold	72,000
Book value of Machinery sold	33,000
Add : Profit on Sale : 20% of ₹33,000	6,600
Proceeds from sale of Machinery	39,600

(4)

Dr. PLANT & MACHINERY ACCOUNT Cr.

Particulars	₹	Particulars	₹
To Balance b/d	8,50,000	By Bank (Sale)	39,600
To Gain on the sale of machinery	6,600	By Accumulated Dep. A/c (Being accumulated depreciation on machinery sold)	72,000
To Bank A/c (Balancing figure, being purchase)	1,87,000	By Balance c/d	9,32,000
	10,43,600		10,43,600

ILLUSTRATION 26.

Hero Ltd. had the following balances :

Non-Current Investments on 31st March, 2021 ₹3,40,000
Non-Current Investments on 31st March, 2022 ₹2,80,000

During the year the company had sold 40% of its original investments at a profit of ₹84,000.

Calculate sources and uses of cash.

SOLUTION :

Sources :

		₹
40% of ₹3,40,000	=	1,36,000
+ Profit	=	84,000
		2,20,000

Uses : Non-Current Investments A/c should be prepared to find out the uses of Cash :

Dr. NON CURRENT INVESTMENTS A/C Cr.

Date	Particulars	Amount	Date	Particulars	Amount
		₹			₹
1.4.2021	To Balance b/d	3,40,000	During 2021-22	By Bank A/c	2,20,000
During 2021-22	To Gain on Sale of Non-Current Investments	84,000	31-3-2022	By Balance c/d (Given)	2,80,000
	To Bank A/c (Balancing figure, being purchase)	76,000			
		5,00,000			5,00,000

Therefore, Uses of Cash (purchase of Non-Current Investments) = ₹76,000.

ILLUSTRATION 27.

From the following particulars of Bharat Gas Limited, calculate Cash Flows from Investing Activities. Also show the workings clearly preparing the ledger accounts.

Assets	31-3-2017	31-3-2018
	₹	₹
Goodwill	1,00,000	3,00,000

Patents	2,80,000	1,60,000
Machinery	10,20,000	12,40,000
10% Long term investment	60,000	1,60,000
Investment in land	1,00,000	1,00,000
Shares of Amartax Ltd.	1,00,000	1,00,000

Additional Information :

1. Patents were written off to the extent of ₹40,000 and some Patents were sold at a profit of ₹20,000.
2. A Machine costing ₹1,40,000 (Depreciation provided thereon ₹60,000) was sold for ₹50,000. Depreciation charged during the year was ₹1,40,000.
3. On March 31, 2018, 10% Investments were purchased for ₹1,80,000 and some Investments were sold at a profit of ₹20,000. Interest on Investment was received on March 31, 2018.
4. Amartax Ltd. paid Dividend @ 10% on its shares.
5. A plot of Land was purchased out of surplus funds for investment purposes and let out for commercial use and rent received ₹30,000.

SOLUTION : CASH FLOWS FROM INVESTING ACTIVITIES

	₹
Purchase of Goodwill	(2,00,000)
Proceeds from sale of Patents (See Note 1)	1,00,000
Proceeds from sale of Machinery	50,000
Purchase of Machinery (See Note 2)	(4,40,000)
Purchase of 10% Investments	(1,80,000)
Proceeds from sale of Investments (See Note 3)	1,00,000
Interest received (10% on ₹60,000)	6,000
Dividend Received (10% on ₹1,00,000)	10,000
Rent received	30,000
Net Cash used in Investing Activities	(5,24,000)

Working Notes : (1)

Dr. PATENTS ACCOUNT Cr.

Particulars	₹	*Particulars*	₹
To Balance b/d	2,80,000	By Statement of P & L (Written off)	40,000
To Gain on Sale	20,000	By Bank A/c (Balancing figure, being sale of patents)	1,00,000
		By Balance c/d	1,60,000
	3,00,000		3,00,000

(2)

Dr. MACHINERY ACCOUNT Cr.

Particulars	₹	*Particulars*	₹
To Balance b/d	10,20,000	By Depreciation A/c	1,40,000
To Bank A/c (Balancing figure,		By Bank A/c (Sale)	50,000

being purchase)	4,40,000	By Loss on sale (1,40,000 – 60,000 – 50,000)	30,000
		By Balance c/d	12,40,000
	14,60,000		14,60,000

(3)

Dr. 10% INVESTMENTS ACCOUNT Cr.

Particulars	₹	Particulars	₹
To Balance b/d	60,000	By Bank A/c (Balancing figure, being sale)	1,00,000
To Bank A/c (Purchases)	1,80,000	By Balance c/d	1,60,000
To Gain on Sale	20,000		
	2,60,000		2,60,000

Cash Flows from Financing Activities

ILLUSTRATION 28.

From the following activities, calculate cash flows from financing activities :

	31.3.2018 ₹	31.3.2017 ₹
Equity Share Capital	8,00,000	6,00,000
12% Preference Share Capital	—	2,00,000
14% Debentures	1,00,000	—

Additional Information :

(*i*) Equity Shares were issued at a premium of 15%.

(*ii*) 12% Preference Shares were redeemed at a premium of 5%.

(*iii*) 14% debentures were issued at a discount of 1%.

(*iv*) Dividend paid on old Preference Shares ₹24,000.

(*v*) Interest paid on debentures ₹14,000.

(*vi*) Underwriting commission of Equity Shares ₹10,000.

(*vii*) Proposed Dividend on Equity Shares for the year ended 31.3.2018 ₹1,20,000.

(*viii*) Proposed Dividend on Equity Shares for the year ended 31.3.2017 ₹90,000.

SOLUTION : CASH FLOWS FROM FINANCING ACTIVITIES

	₹
Proceeds from issue of Equity Share Capital (₹2,00,000 + Securities Premium ₹30,000 – Underwriting Commission ₹10,000)	2,20,000
Redemption of Preference Shares (₹2,00,000 + Premium on Redemption ₹10,000)	(2,10,000)
Proceeds from issue of Debentures (₹1,00,000 – ₹1,000)	99,000
Proposed Dividend on Equity Shares for the year ended 31st March, 2017	(90,000)
Dividend paid on Preference Shares	(24,000)
Interest paid on Debentures	(14,000)
Net Cash used in Financing Activities	(19,000)

Notes :

(*i*) Proposed Dividend for Previous Year *i.e.*, for the year ended 31st March, 2017 is declared (approved) in the year ended 31st March 2018. Hence it will be added back to Net Profit to determine net profit before tax. It will also be shown under financing activities as Outflow of Cash.

(*ii*) Proposed Dividend for Current Year *i.e.*, for the year ended 31st March 2018 will be declared (approved) in the next financial year. Hence, it will have no effect on Cash Flow Statement.

ILLUSTRATION 29.

From the following extracts taken from the Balance Sheets of M/s Khanduja Ltd., on 31st March and the additional information provided, you are required to calculate :

(*i*) Cash Flows from Operating Activities.

(*ii*) Cash Flows from Financing Activities.

Equity & Liabilities	*31.3.2021*	*31.3.2022*
	₹	₹
Equity Share Capital	20,00,000	30,00,000
10% Preference Share Capital	2,00,000	1,00,000
Securities Premium Reserve A/c	—	95,000
Profit and Loss Balance	4,00,000	8,00,000
10% Debentures	10,00,000	10,00,000

Additional Information :

1. Fresh equity shares were issued on 31st March 2022 at a premium of 10%.
2. Interim Dividend was paid on equity shares @8%.
3. Preference shares were redeemed on 31st March, 2022 at premium of 5%. Premium on redemption was charged against premium received on issue of fresh equity shares.

SOLUTION : (*i*) CASH FLOWS FROM OPERATING ACTIVITIES

Particulars	₹	₹
Net Profit before Tax (Note 1)	5,80,000	
Adjustments for non-cash and non-operating items :		
Add : Interest on Debentures	1,00,000	
Net Cash flows from Operating Activities	6,80,000	6,80,000

Note : (1) Calculation of Net Profit before Tax :

	₹
Profit & Loss Balance on 31st March, 2022	8,00,000
Less : Profit & Loss Balance on 31st March, 2021	4,00,000
	4,00,000
Add : Dividend on Preference Shares (10% on ₹2,00,000)*	20,000
Dividend on Equity Shares (8% on ₹20,00,000)	1,60,000
	5,80,000

(ii) CASH FLOWS FROM FINANCING ACTIVITIES

Particulars	₹	₹
Cash Proceeds from Issue of Equity Shares (₹10,00,000 + Securities Premium Reserve ₹1,00,000)	11,00,000	
Cash paid for Redemption of Preference Shares (₹1,00,000 + Premium ₹5,000)	(1,05,000)	
Dividend paid on Preference Shares	(20,000)	
Dividend paid on Equity Shares	(1,60,000)	
Interest on Debentures	(1,00,000)	
Net Cash flows from Financing Activities	7,15,000	7,15,000

* Dividend on Pref. Shares is paid before payment of dividend on Equity Shares. The Company has paid interim dividend on equity shares. Hence, it must have paid dividend on preference shares.

ILLUSTRATION 30.

From the following information of *X* Ltd., Calculate Cash flows from financing activities :

Particulars	*31st March, 2018*	*31st March, 2017*
	₹	₹
Equity Share Capital	30,00,000	20,00,000
12% Debentures	—	3,00,000
10% Debentures	5,00,000	—
Bank Overdraft	80,000	1,00,000

Additional Information :

(*i*) During the year 2017-18, *X* Ltd. issued bonus shares in the ratio of 2 : 1 by capitalising reserve.

(*ii*) 12% Debentures were redeemed on 1st July 2017 and new 10% Debentures were issued on the same date at a discount of 5%.

(*iii*) Proposed Dividend on equity share capital for previous year ended 31st March 2017 was paid @ 8%.

(*iv*) Interest paid on Bank Overdraft ₹10,000.

SOLUTION : CASH FLOWS FROM FINANCING ACTIVITIES

Particulars	₹
Redemption of 12% Debentures	(3,00,000)
Proceeds from Issue of 10% Debentures (₹5,00,000 – ₹25,000 Discount)	4,75,000
Interest Paid on Debentures (Note 2)	(46,500)
Decrease in Bank Overdraft	(20,000)
Proposed Dividend paid on Equity Share Capital (8% on ₹20,00,000)	(1,60,000)
Interest Paid on Bank Overdraft	(10,000)
Net Cash used in Financing Activities	(61,500)

Notes :

(1) Bonus Shares are issued to existing equity shareholders without charging any amount from them. Hence, bonus shares are not shown in Cash Flow Statement because there is no flow of Cash. Bonus shares are issued in the ratio of 2 : 1. It means a shareholder holding 2 shares is issued 1 bonus share. As such, ₹10,00,000 bonus shares are issued.

(2) Interest on Debentures :

12% on ₹3,00,000 for 3 months	=	₹ 9,000
10% on ₹5,00,000 for 9 months	=	₹ 37,500
		₹ 46,500

ILLUSTRATION 31.

From the following information, Calculate :

(*i*) Cash Flows from Investing Activities, and

(*ii*) Cash Flows from Financing Activities.

Particulars	*31st March, 2018*	*31st March, 2017*
	₹	₹
Plant & Machinery	6,80,000	5,60,000
Accumulated Depreciation on Plant & Machinery	1,70,000	1,48,000
Equity Share Capital	12,00,000	10,00,000
Loan from Bank	2,00,000	1,50,000

Additional Information :

(*i*) During the year a machine costing ₹1,20,000 was sold at a profit of ₹15,000. Depreciation on Plant & Machinery charged during the year amounted to ₹50,000.

(*ii*) Interest paid on Bank Loan amounted to ₹30,000.

(*iii*) Dividend paid ₹80,000.

SOLUTION : CASH FLOWS FROM INVESTING ACTIVITIES

Particulars	₹
Sale of Machinery (Working Note 3)	1,07,000
Purchase of Machinery	(2,40,000)
Net Cash used in Investing Activities	(1,33,000)

CASH FLOWS FROM FINANCING ACTIVITIES

Particulars	₹
Proceeds from Issue of Equity Share Capital	2,00,000
Proceeds from Bank Loan	50,000
Interest paid on Bank Loan	(30,000)
Dividend Paid	(80,000)
Net Cash Flows from Financing Activities	1,40,000

Working Notes :

(1)

Dr. ACCUMULATED DEPRECIATION ACCOUNT Cr.

Particulars	₹	Particulars	₹
To Plant & Machinery A/c (Balancing figure, being the accumulated depreciation on machinery sold)	28,000	By Balance b/d	1,48,000
To Balance c/d	1,70,000	By Depreciation A/c	50,000
	1,98,000		1,98,000

(2)

Dr PLANT & MACHINERY ACCOUNT Cr.

Particulars	₹	Particulars	₹
To Balance b/d	5,60,000	By Bank A/c (Sale) (Working Note 3)	1,07,000
To Gain on Sale of Machinery	15,000	By Accumulated Dep. A/c (being accumulated depreciation on machinery sold)*	28,000
To Bank A/c (Balancing Figure, being purchase)	2,40,000	By Balance c/d	6,80,000
	8,15,000		8,15,000

(3) Sale Price of Machinery :
Cost of Machinery – Accumulated Dep. + Profit on Sale
₹1,20,000 – ₹28,000 + ₹15,000 = ₹1,07,000

*This amount has been transferred from Accumulated Depreciation A/c.

Preparation of Cash-Flow Statement

Net cash from operating activities is to be shown under part 'A' of the cash flow statement.

Total of Part A, B and C will be the net increase or decrease in cash and cash equivalents during the period. If the balance of cash and cash equivalents at the beginning is added to this figure, it will amount to the balance of cash and cash equivalents at the end of the period and hence the accuracy of the solution stands automatically verified.

Provision for Income-Tax :

(*i*) 'Provision for Income-Tax' appearing on the liabilities side of previous year's balance sheet will be treated as payment of tax during the year. Hence it will be deducted while calculating net cash from operating activities.

(*ii*) 'Provision for Income-Tax' appearing on the liabilities side of current year's balance sheet will be added back to profits because 'net profit before taxation' is to be shown under the heading 'Cash flow from operating activities'.

Proposed Dividend :

According to Revised AS-4, Contingencies and Events Occurring after the Balance Sheet date, Proposed Dividend is not provided in the books but is shown in the notes to accounts as Contingent Liability. In other words, it will not appear as Short Term Provision on the Liabilities side of the Balance Sheet.

The effect of Proposed Dividend on Cash Flow Statement will be as follows :

(*i*) **Proposed dividend for Previous Year** : It will be shown as Outflow of Cash in Financing activities assuming it has been declared (approved) at the Annual General Meeting of Shareholders in the Current year.

It will also be added to Net Profit for determining the Net Profit before Tax.

(*ii*) **Proposed Dividend for the Current Year** : There will be no effect of Proposed Dividend of Current Year on Cash Flow Statement because it will be declared (approved) at the Annual General Meeting of Shareholders to be held after the end of financial year *i.e.*, in the next financial year.

ILLUSTRATION 32.

Following are the Balance Sheets of *X* Ltd. for two years. Prepare a Cash Flow Statement :

Particulars	*Note No.*	*31.3.2022*	*31.3.2021*
I. EQUITY AND LIABILITIES :		₹	₹
(1) Shareholder's Funds :			
(*a*) Share Capital		3,00,000	2,00,000
(*b*) Reserve & Surplus		80,000	30,000
(2) Non-Current Liabilities :			
Long-term Borrowings	1	—	75,000
(3) Current Liabilities :			
(*a*) Short-term Borrowings	2	25,000	37,000
(*b*) Trade Payables		1,50,000	96,000
(*c*) Short term Provisions (Provision for Tax)		15,000	12,000
TOTAL		5,70,000	4,50,000
II. ASSETS :			
(1) Non-Current Assets :			
Fixed Assets	3	3,40,000	3,00,000
(2) Current Assets :			
(*a*) Current Investments (Short-term Investments)		30,000	20,000
(*b*) Inventory		90,000	60,000
(*c*) Trade Receivables		97,000	65,000
(*d*) Cash & Bank Balances		13,000	5,000
TOTAL		5,70,000	4,50,000

Notes : (1) Long-term Borrowings :	*31.3.2022*	*31.3.2021*
	₹	₹
15% Loan	—	75,000

(2) Short-term Borrowings :		
Bank Overdraft	25,000	37,000
(3) Fixed Assets :		
Plant & Machinery	4,00,000	3,50,000
Less : Accumulated Depreciation	60,000	50,000
	3,40,000	3,00,000

Additional Information :

(1) Contingent Liability :	*31.3.2022*	*31.3.2021*
	₹	₹
Proposed Dividend	30,000	20,000

(2) Loan was repaid on 1st April, 2021.

SOLUTION :

CASH FLOW STATEMENT

for the year ended 31st March, 2022

Particulars		₹	₹
A. Cash flows from Operating Activities :			
Net profit before Tax (Note 1)		85,000	
Adjustments for non-cash and non-operating items :			
Add : Depreciation on Plant & Machinery(3)		10,000	
Operating profit before working capital changes		95,000	
Add : Increase in Current Liabilities :			
Trade Payables		54,000	
		1,49,000	
Less : Increase in Current Assets :			
Inventory	30,000		
Trade Receivables	32,000	62,000	
		87,000	
Payment of Tax (for the year 2021)		12,000	
Net cash from operating activities		75,000	75,000
B. Cash flows from Investing Activities :			
Purchase of Plant & Machinery (2)		(50,000)	
Net cash used in investing activities		(50,000)	(50,000)
C. Cash flows from Financing Activities :			
Issue of Share Capital		1,00,000	
Repayment of loan		(75,000)	
Repayment of Short term Borrowings (Bank Overdraft)(5)		(12,000)	
Payment of Proposed Dividend (for 2021)		(20,000)	
Net cash used in financing activities		(7,000)	(7,000)
Net increase in cash and cash equivalents			18,000
Add : Cash and cash equivalents in the beginning of the period(4)			25,000
Cash and cash equivalents at the end of the period			43,000

Notes : (1) Calculation of Net Profit before Tax :

		₹
	Reserve & Surplus Balance on 31st March, 2022	80,000
Less :	Reserve & Surplus Balance on 31st March, 2021	30,000
		50,000
Add :	Proposed Dividend for Previous year*	20,000
	Provision for Tax made during the Current year	15,000
Net Profit before Tax		85,000

* Proposed Dividend for previous year (*i.e.*, 2021) will be added to Net Profit before Tax and will also be shown as Outflow under financing activities. There will be no effect of proposed dividend of Current year (*i.e.*, 2022)

(2)

PLANT & MACHINERY A/C

(On Original Cost)

Dr. Cr.

Particulars	₹	*Particulars*	₹
To Balance b/d (Given)	3,50,000		
To Bank A/c (Balancing figure, being purchase)	50,000	By Balance c/d (Given)	4,00,000
	4,00,000		4,00,000

(3)

ACCUMULATED DEPRECIATION A/C

Dr. Cr.

Particulars	₹	*Particulars*	₹
		By Balance b/d (2021 Balance)	50,000
To Balance c/d (2022 Balance)	60,000	By Depreciation A/c (Balancing figure, being Current year's Depreciation)	10,000
	60,000		60,000

It is important to note that if the balances of fixed assets account and provision for depreciation account are given separately in the question, the students are advised to prepare the two accounts separately.

(4)

	31.3.2022	*31.3.2021*
	₹	₹
Cash and Cash Equivalents :		
Cash and Bank Balances	13,000	5,000
Current Investments	30,000	20,000
	43,000	25,000

(5) As per ISC Council's instructions, Bank Overdraft and Cash Credit will be treated as 'Short-term Borrowings' and as per Para 17 of AS-3 (Revised) Cash proceeds from short term borrowings should be classified under Financing Activities. As such, Bank Overdraft and Cash Credit will be treated as 'Financing Activities' instead of Cash Equivalents.

ILLUSTRATION 33.

Following is the Balance Sheet of R.S. Ltd. as at 31st March, 2018 :

R.S. Ltd. Balance Sheet as at 31-3-2018

Particulars	*Note No.*	*31-3-2018* ₹	*31-3-2017* ₹
I. Equity and Liabilities			
(1) Shareholder's Funds			
(*a*) Share Capital		9,00,000	7,00,000
(*b*) Reserves and Surplus		2,50,000	1,00,000
(2) Non-current Liabilities			
Long-term borrowings (12% Debentures)		4,50,000	3,50,000
(3) Current Liabilities			
(*a*) Short-term borrowings	1	1,50,000	75,000
(*b*) Trade Payables		2,00,000	1,25,000
		19,50,000	13,50,000
II. Assets			
(1) Non-current Assets			
(*a*) Fixed Assets			
(*i*) Tangible	2	14,65,000	9,15,000
(*ii*) Intangible (Goodwill)		1,00,000	1,50,000
(*b*) Non-current Investments		1,50,000	1,00,000
(2) Current Assets			
(*a*) Current Investments		40,000	70,000
(*b*) Inventories		1,22,000	72,000
(*c*) Cash and Bank Balances		73,000	43,000
Total		19,50,000	13,50,000

Notes to Accounts :

Note No.	*Particulars*	*31-3-2018* ₹	*31-3-2017* ₹
1.	Short-term borrowings — Bank overdraft	1,50,000	75,000
2.	Tangible Assets		
	Machinery	16,75,000	10,55,000
	Accumulated Depreciation	(2,10,000)	(1,40,000)
		14,65,000	9,15,000

Additional Information :

	31.3.2018 ₹	*31.3.2017* ₹
(1) Contingent Liability :		
Proposed Dividend	2,00,000	1,25,000

(2) ₹1,00,000, 12% Debentures were issued on 31-3-2018.

(3) During the year a piece of machinery costing ₹80,000, on which accumulated depreciation was ₹40,000, was sold at a loss of ₹10,000.

Prepare a Cash Flow Statement.

SOLUTION :

R.S Limited
CASH FLOW STATEMENT *for the year ended 31st March, 2018*

Particulars		*Amount* ₹	*Amount* ₹
I. CASH FLOW FROM OPERATING ACTIVITIES			
Net Profit before tax (Note 1)		2,75,000	
Adjustment for Non-Cash and Non-Operating Items :			
Depreciation	1,10,000		
Loss on Sale of Machinery	10,000		
Interest on Debentures (12% on ₹3,50,000)	42,000		
Goodwill Written off	50,000	2,12,000	
Operating Profit before changes in working capital		4,87,000	
Add : Decrease in Current Assets and Increase in Current Liabilities :			
Current Investments*	30,000		
Trade Payables	75,000	1,05,000	
		5,92,000	
Less : Increase in Current Assets and Decrease in Current Liabilities : Stock in Trade		50,000	
Cash Flow from Operating Activities		5,42,000	5,42,000
II. CASH FLOW FROM INVESTING ACTIVITIES			
Purchase of Machinery		(7,00,000)	
Sale of Machinery		30,000	
Purchase of Non-Current Investments		(50,000)	
Cash Used in Investing Activities		(7,20,000)	(7,20,000)
III. CASH FLOW FROM FINANCING ACTIVITIES			
Issue of Share Capital		2,00,000	
Issue of 12% Debentures		1,00,000	
Interest paid on Debentures		(42,000)	
Increase in Bank Overdraft		75,000	
Payment of Proposed Dividend (for 2017)		(1,25,000)	
Cash Flow from Financing Activities		2,08,000	2,08,000
Net Increase/Decrease in Cash & Cash Equivalents			30,000
Add : Opening Balance of Cash and Cash Equivalents			43,000
Closing Balance of Cash and Cash Equivalents			73,000

Dr. **PLANT & MACHINERY A/C** Cr.

Particulars	*Amount* ₹	*Particulars*	*Amount* ₹
To Balance b/d	10,55,000	By Bank A/c	30,000
To Bank A/c (Balancing figure, being purchase)	7,00,000	By Accumulated Depreciation A/c	40,000
		By Loss on Sale	10,000

		By Balance c/d	16,75,000
	17,55,000		17,55,000

Dr. **ACCUMULATED DEPRECIATION A/C** Cr.

Particulars	*Amount*	*Particulars*	*Amount*
	₹		₹
To Plant & Machinery A/c	40,000	By Balance b/d	1,40,000
To Balance c/d	2,10,000	By Depreciation A/c (Balancing Figure)	1,10,000
	2,50,000		2,50,000

Working Notes :

(1) Calculation of Net Profit before Tax :

	₹
Reserve & Surplus Balance on 31.3.2018	2,50,000
Less : Reserve & Surplus Balance on 31.3.2017	1,00,000
	1,50,000
Add : Proposed Dividend for Previous Year**	1,25,000
	2,75,000

* As per I.S.C. Guidelines Current Investments are included in Working Capital while Short term Investments or Marketable Securities are included in Cash and Cash Equivalents.

** Proposed Dividend for previous year will be added to net profit before tax and will also be shown as Outflow under financing activities. There will be no effect of Proposed Dividend of Current Year.

Preparation of Provision for Tax Account

Case I : Sometimes Opening and Closing amounts of Provision for Tax are given in the question and actual tax paid during the year is also given in additional information. In such a case 'Provision for Tax A/c' has to be prepared to ascertain the amount of provision for tax made during the current year.

ILLUSTRATION 34.

Prepare 'Provision for Income Tax Account' from the following informations for preparing Cash Flow Statement :

EQUITY AND LIABILITY SIDE OF BALANCE SHEET

	31-03-2021	*31-03-2022*
	₹	₹
Provision for Income Tax	3,20,000	4,00,000

Additional Information :

During the year Income Tax paid was ₹2,80,000.

SOLUTION :

Dr. PROVISION FOR INCOME TAX ACCOUNT Cr.

Particulars	₹	*Particulars*	₹
To Bank A/c (Payment made)		By Balance b/d (Given)	3,20,000

(Given)	2,80,000	By Statement of P & L	
To Balance c/d (Given)	4,00,000	(Balancing figure, being provision made in 2022)	3,60,000
	6,80,000		6,80,000

Case II. In Case Opening and Closing amounts of Provision for Tax are given in the question and Provision for Tax made during current year is also given, then 'Provision for Tax A/c' must be prepared to find out the figure of actual tax paid during the current year.

ILLUSTRATION 35.

Prepare 'Provision for Income Tax Account' from the following informations for preparing Cash Flow Statement :

EQUITY AND LIABILITY SIDE OF BALANCE SHEET

	31-03-2021 ₹	31-03-2022 ₹
Provision for Income Tax	1,50,000	2,10,000

Additional Information :

Provision for Income Tax made during the year 2022 was ₹2,35,000.

SOLUTION :

Dr. PROVISION FOR INCOME TAX ACCOUNT Cr.

Particulars	₹	*Particulars*	₹
To Bank A/c (balancing figure, being payment made)	1,75,000	By Balance b/d (Given)	1,50,000
To Balance c/d (Given)	2,10,000	By Statement of P & L (Provision made in 2022) (Given)	2,35,000
	3,85,000		3,85,000

ILLUSTRATION 36.

You are required to prepare a Cash-Flow Statement (as per AS-3) for the year 2016-17 from the following Balance Sheets.

Balance Sheets of Honesty Ltd.
as at 31st March, 2016 and 31st March, 2017

Particulars	*Note No.*	*31-3-2017* ₹	*31-3-2016* ₹
I. EQUITY AND LIABILITIES :			
(1) Shareholder's Funds :			
(*a*) Share Capital (Equity Share Capital)		14,00,000	10,00,000
(*b*) Reserve and Surplus (Statement of P&L)		5,00,000	4,00,000
(2) Non-Current Liabilities :			
Long Term Borrowings (10% Debentures)		5,00,000	1,40,000
(3) Current Liabilities :			
(*a*) Short Term Borrowings (Bank Overdraft)		20,000	30,000

(*b*) Trade Payables (Creditors)		1,00,000	60,000
(*c*) Short Term Provisions	1	60,000	30,000
TOTAL		25,80,000	16,60,000
II. ASSETS :			
(1) Non-Current Assets :			
Fixed Assets :			
(*i*) Tangible	2	16,00,000	9,00,000
(*ii*) Intangible (Goodwill)		1,40,000	2,00,000
(2) Current Assets :			
(*a*) Inventory		2,50,000	2,00,000
(*b*) Trade Receivables		5,00,000	3,00,000
(*c*) Cash & Bank Balances (Cash at Bank)		90,000	60,000
TOTAL		25,80,000	16,60,000

Notes to Accounts :

Particulars	*31-3-2017* ₹	*31-3-2016* ₹
1. **Short term provisions :**		
Provision for taxation	60,000	30,000
2. **Fixed Assets (Tangible) :**		
Plant and Machinery	17,60,000	10,00,000
Less : Accumulated Depreciation	(1,60,000)	(1,00,000)
	16,00,000	9,00,000

Additional Information :

During the year 2016-17 :

(*i*) A part of the machine, costing ₹50,000, accumulated depreciation thereon being ₹20,000, was sold for ₹18,000.

(*ii*) Tax paid ₹20,000.

(*iii*) Interest paid on Debentures ₹50,000 . *(I.S.C. 2018)*

SOLUTION :

Honesty Ltd.

CASH FLOW STATEMENT

for the year ended 31st March, 2017

Particulars		₹	₹
A. Cash flows from Operating Activities :			
Net profit before Tax (Note 1)		1,50,000	
Add : Non-operating/non-cash expenses			
Goodwill written off		60,000	
Depreciation on Plant & Machinery$^{(3)}$		80,000	
Loss on Sale of Plant & Machinery		12,000	
Interest on Debentures		50,000	
Net Operating Profit before working capital charges		3,52,000	
Add : Increase in Trade Payables	40,000		

Less : Increase in Inventory	(50,000)		
Less : Increase in Trade Receivables	(2,00,000)	(2,10,000)	
Cash Flow from operating activities before tax paid		1,42,000	
Less : Tax Paid		(20,000)	
Cash Flow from Operating Activities		1,22,000	1,22,000
B. Cash flows from Investing Activities :			
Sale of Plant & Machinery		18,000	
Purchase of Plant & Machinery(2)		(8,10,000)	
Cash used in Investing Activities		(7,92,000)	(7,92,000)
C. Cash flows from Financing Activities :			
Issue of Equity Share Capital		4,00,000	
Issue of Debentures		3,60,000	
Interest paid on Debentures		(50,000)	
Bank Overdraft repaid		(10,000)	
Cash Flow from Financing Activities		7,00,000	7,00,000
Net increase in Cash and Cash Equivalents			30,000
Add : Cash & Cash Equivalents in the beginning			60,000
Cash & Cash Equivalents at the end			90,000

Working Notes :

(1) Calculation of Net Profit before Tax :

	₹
Net Profit for the year (₹5,00,000 – ₹4,00,000)	1,00,000
Add : Provision for Tax(4)	50,000
Net Profit before Tax	1,50,000

(2)

Dr. PLANT AND MACHINERY ACCOUNT Cr.

Particulars	₹	*Particulars*	₹
To Balance b/d	10,00,000	By Bank A/c	18,000
To Bank A/c (Balancing figure, being purchase)	8,10,000	By Accumulated Depreciation A/c	20,000
		By Loss on Sale	12,000
		By Balance c/d	17,60,000
	18,10,000		18,10,000

(3)

Dr. ACCUMULATED DEPRECIATION ACCOUNT Cr.

Particulars	₹	*Particulars*	₹
To Plant & Machinery A/c	20,000	By Balance b/d	1,00,000
To Balance c/d	1,60,000	By Depreciation A/c (Bal. figure, being current year's depreciation)	80,000
	1,80,000		1,80,000

(4)

Dr. PROVISION FOR TAXATION ACCOUNT Cr.

Particulars	₹	*Particulars*	₹
To Bank A/c (Given)	20,000	By Balance b/d	30,000
To Balance c/d	60,000	By Statement of Profit & Loss (Balancing figure, being provision made)	50,000
	80,000		80,000

ILLUSTRATION 37.

Following are the Balance Sheets of *X* Ltd. :

BALANCE SHEET *as at* ....

Particulars	*Note No.*	*31.3.2019*	*31.3.2018*
I. EQUITY AND LIABILITIES :		₹	₹
(1) Shareholder's Funds :			
(*a*) Share Capital		4,50,000	4,50,000
(*b*) Reserve & Surplus	1	4,78,000	3,56,000
(2) Non-Current Liabilities :			
Long-term Borrowings	2	1,70,000	—
(3) Current Liabilities :			
(*a*) Trade Payables		1,09,000	2,03,000
(*b*) Short term Provision	3	35,000	40,000
TOTAL		12,42,000	10,49,000
II. ASSETS :			
(1) Non-Current Assets :			
Fixed Assets :			
(*i*) Tangible Assets	4	3,20,000	4,00,000
(*ii*) Intangible Assets	5	60,000	50,000
(2) Current Assets :			
(*a*) Current Investments (Short-term)		70,000	78,000
(*b*) Inventory		1,70,000	2,15,000
(*c*) Trade Receivables		4,55,000	2,10,000
(*d*) Cash and Bank		1,67,000	96,000
TOTAL		12,42,000	10,49,000

	31.3.2019	*31.3.2018*
Notes : (1) Reserve & Surplus :	₹	₹
Retained Earnings	4,78,000	3,56,000
(2) Long-term Borrowings : Mortgage Loan	1,70,000	—
(3) Short term Provision : Provision for Taxation	35,000	40,000

(4) Tangible Assets :		
Land	1,40,000	2,50,000
Plant & Machinery	1,80,000	1,50,000
	3,20,000	4,00,000
(5) Intangible Assets :		
Goodwill	60,000	50,000

Additional Information :—

(*i*) Gain on sale of Land ₹30,000.

(*ii*) Depreciation on Plant & Machinery was provided at 10% on last year's balance.

(*iii*) Interest paid on Mortgage Loan amounted to ₹24,300.

(*iv*) Provision for Income Tax made during the year 2018-19 was ₹32,000.

SOLUTION :

CASH FLOW STATEMENT

for the year ended 31st March, 2019

Particulars		₹	₹
A. Cash flows from Operating Activities :			
Net profit before Tax (Note 1)		1,54,000	
Adjustments for non-cash and non-operating items :			
Add : Depreciation on Plant & Machinery		15,000	
Interest paid on Mortgage Loan		24,300	
		1,93,300	
Less : Gain on sale of land		30,000	
Operating profit before working capital changes		1,63,300	
Add : Decrease in Current Assets :			
Inventory		45,000	
		2,08,300	
Less : Increase in Current Assets :			
Trade Receivables	2,45,000		
Decrease in Current Liabilities :			
Trade Payables	94,000	3,39,000	
		(1,30,700)	
Less : Income Tax paid for 2018(5)		(37,000)	
Net cash used in operating activities		(1,67,700)	(1,67,700)
B. Cash flows from Investing Activities :			
Purchase of Plant & Machinery(2)		(45,000)	
Purchase of Goodwill(3)		(10,000)	
Sale of Land(4)		1,40,000	
Net cash from investing activities		85,000	85,000
C. Cash flows from Financing Activities :			
Proceeds from Mortgage Loan		1,70,000	

Interest on Mortgage Loan	(24,300)	
Net cash from financing activities	1,45,700	1,45,700
Net increase in cash and cash equivalents		63,000
Add : Cash and cash equivalents in the beginning of the period(6)		1,74,000
Cash and cash equivalents at the end of the period(6)		2,37,000

Notes : (1) Calculation of Net Profit before Tax :

	₹
Retained Earnings on 31st March, 2019	4,78,000
Less : Retained Earnings on 31st March, 2018	3,56,000
	1,22,000
Add : Provision for tax made during the Current year	32,000
Net Profit before Tax	1,54,000

(2) PLANT & MACHINERY ACCOUNT

(On written down value)

Dr. Cr.

Particulars	₹	*Particulars*	₹
To Balance b/d	1,50,000	By Depreciation	15,000
To Bank A/c (Balancing figure, being purchase)	45,000	By Balance c/d	1,80,000
	1,95,000		1,95,000

(3) Increase in Goodwill will be treated as purchase of Goodwill.

(4)

LAND ACCOUNT

Dr. Cr.

Particulars	₹	*Particulars*	₹
To Balance b/d	2,50,000	By Bank A/c (Balancing figure, being sale)	1,40,000
To Gain on Sale	30,000	By Balance c/d	1,40,000
	2,80,000		2,80,000

(5)

PROVISION FOR TAX ACCOUNT

Dr. Cr.

Particulars	₹	*Particulars*	₹
To Bank A/c (Balancing figure, being payment made)	37,000	By Balance b/d	40,000
To Balance c/d	35,000	By Statement of Profit & Loss (Provision made) (Given)	32,000
	72,000		72,000

(6) Cash and Cash Equivalents :

	31-3-2019 (₹)	*31-3-2018* (₹)
Cash and Bank	1,67,000	96,000
Current Investments (Short-term)	70,000	78,000
	2,37,000	1,74,000

ILLUSTRATION 38.

The Balance Sheets of Rajneesh Ltd., for the years ending on 31st March 2019 and 2018 were as follows :

Particulars	*Note No.*	*2019*	*2018*
		₹	₹
I. EQUITY AND LIABILITIES :			
(1) **Shareholder's Funds :**			
(*a*) Share Capital		1,25,000	1,00,000
(*b*) Reserve and Surplus	1	33,800	30,250
(2) **Non-Current Liabilities :**			
Long-Term Borrowings		7,500	10,000
(3) **Current Liabilities :**			
(*a*) Short-term Borrowings	2	—	35,000
(*b*) Trade Payables		72,600	75,000
(*c*) Short-term Provisions	3	16,500	15,000
TOTAL		2,55,400	2,65,250
II. ASSETS :			
(1) **Non-Current Assets :**			
Fixed Assets	4	1,82,000	1,75,000
(2) **Current Assets :**			
(*a*) Inventories		37,000	50,000
(*b*) Trade Receivables		32,100	40,000
(*c*) Cash and Bank Balances	5	4,300	250
TOTAL		2,55,400	2,65,250

otes :	*2019* (₹)	*2018* (₹)
(1) Reserve and Surplus :		
Profit & Loss Balance	33,800	30,250
(2) Short-term Borrowings :		
Bank Overdraft	—	35,000
(3) Short-term Provisions :		
Provision for Tax	16,500	15,000
(4) Fixed Assets :		
Land & Buildings	95,000	1,00,000
Plant & Machinery	87,000	75,000
	1,82,000	1,75,000
(5) Cash & Bank Balances :		
Cash in hand	300	250
Bank Balance	4,000	—
	4,300	250

dditional Information :

(*i*) Depreciation written off on Land & Buildings during the year 2018-19 was ₹6,000.

(*ii*) Land was purchased for ₹19,000 during the year 2018-19.

Prepare the Cash Flow Statement of Rajneesh Ltd.

SOLUTION :

CASH FLOW STATEMENT

for the year ended 31st March, 2019

Particulars		₹	₹
A. Cash flows from Operating Activities :			
Net profit before Tax (Note 1)		20,050	
Adjustments for non-cash and non-operating items :			
Add : Depreciation on Land & Buildings		6,000	
Operating profit before working capital changes		26,050	
Add : Decrease in Current Assets :			
Inventories	13,000		
Trade Receivables	7,900	20,900	
		46,950	
Less : Decrease in Current Liabilities :			
Trade Payables		2,400	
		44,550	
Less : Income Tax paid for 2018		(15,000)	
Net Cash from Operating Activities		29,550	29,550
B. Cash Flows from Investing Activities :			
Sale of Land & Buildings(2)		18,000	
Purchase of Land & Buildings		(19,000)	
Purchase of Plant & Machinery		(12,000)	
Net cash used in investing activities		(13,000)	(13,000)
C. Cash Flows from Financing Activities :			
Issue of Share Capital		25,000	
Repayment of Long-term Borrowings		(2,500)	
Repayment of Bank Overdraft		(35,000)	
Net cash used in financing activities		(12,500)	(12,500)
Net increase in cash and cash equivalents			4,050
Add : Cash and Cash equivalents in the beginning of the period(3)			250
Cash and Cash equivalents at the end of the period			4,300

Notes : (1) Calculation of Net Profit before Tax :

	₹
Profit & Loss Balance on 31st March, 2019	33,800
Less : Profit & Loss Balance on 31st March, 2018	30,250
	3,550
Add : Provision for Tax for Current year	16,500
	20,050

(2)

Dr. LAND AND BUILDINGS ACCOUNT Cr.

Particulars	₹	*Particulars*	₹
To Balance b/d	1,00,000	By Depreciation A/c	6,000
To Bank A/c (Purchase)	19,000	By Bank A/c (Balancing figure, being sale)	18,000

		By Balance c/d	95,000
	1,19,000		1,19,000

Payment of Interim Dividend : If interim dividend paid is given in adjustments, it will be added back to profits and will also be shown as payment of cash under the heading 'Cash flows from financing activities'.

ILLUSTRATION 39.

From the following Balance Sheets of Surya Roshni Ltd., as at 31st March 2022 and 2021, prepare a statement of cash flow :

Particulars	*Note No.*	*2022*	*2021*
		₹	₹
I. EQUITY AND LIABILITIES :			
(1) Shareholder's Funds :			
(*a*) Share Capital		4,75,000	4,00,000
(*b*) Reserve and Surplus	1	1,16,000	(30,000)
(2) Non-Current Liabilities :			
Long-term Borrowings	2	2,50,000	2,00,000
(3) Current Liabilities :			
(*a*) Trade Payables		1,10,000	50,000
(*b*) Short term Provision	3	16,000	10,000
TOTAL		9,67,000	6,30,000
II. ASSETS :			
(1) Non-Current Assets :			
(*a*) Fixed Assets	4	4,52,000	1,70,000
(*b*) Non-Current Investments		45,000	40,000
(2) Current Assets :			
(*a*) Current Investments (Short-term)		30,000	50,000
(*b*) Inventory		2,00,000	1,50,000
(*c*) Trade Receivables		56,000	1,76,000
(*d*) Cash & Bank		1,84,000	44,000
TOTAL		9,67,000	6,30,000

Notes :	*2022* (₹)	*2021* (₹)
(1) Reserve & Surplus :		
Securities Premium	60,000	—
Profit & Loss Balance	56,000	(30,000)
	1,16,000	(30,000)
(2) Long-term Borrowings :		
15% Debentures	2,50,000	2,00,000
(3) Short term Provision :		
Provision for Doubtful Debts	14,000	10,000
Provision for Repairs	2,000	—
	16,000	10,000
(4) Fixed Assets :	5,00,000	2,00,000
Less : Accumulated Depreciation	48,000	30,000
	4,52,000	1,70,000

Additional Information :—

I. Interim Dividend paid during the year ₹36,000.
II. Non-Current Investments costing ₹10,000 were sold at a profit of 40%.
III. Tangible Fixed Assets Costing ₹20,000 (accumulated depreciation ₹8,000) were sold for ₹17,000.
IV. Additional debentures amounting to ₹50,000 were issued at par on 1st August 2021. Interest on debentures has been paid regularly.

OLUTION :

CASH FLOW STATEMENT
for the year ended 31st March, 2022

Particulars		₹	₹
. Cash flows from Operating Activities :			
Net profit before Tax (Note 1)		1,22,000	
Adjustments for non-cash and non-operating items :			
Add : Depreciation on fixed tangible assets(3)		26,000	
Provision for doubtful debts		4,000	
Provision for Repairs		2,000	
Interest Paid on Long-term Borrowings (Debentures)		35,000	
		1,89,000	
Less : Profit on sale of non-current investments	4,000		
Profit on sale of fixed tangible assets	5,000	9,000	
Operating profit before working capital changes		1,80,000	
Add : Decrease in Current Assets :			
Trade Receivables	1,20,000		
Increase in Current Liabilities :			
Trade Payables	60,000	1,80,000	
		3,60,000	
Less : Increase in Current Assets :			
Inventory		50,000	
Net cash from operating activities		3,10,000	3,10,000
Cash flows from Investing Activities :			
Purchase of Fixed Tangible Assets(2)		(3,20,000)	
Sale of Fixed Tangible Assets		17,000	
Purchase of Non-Current Investments(4)		(15,000)	
Sale of Non-Current Investments		14,000	
Net cash used in investing activities		(3,04,000)	(3,04,000)
Cash flows from Financing Activities :			
Proceeds from Issue of Share Capital		75,000	
Security Premium received on issue of Share Capital		60,000	
Proceeds from Long term Borrowings (Debentures)		50,000	
Payment of Interim Dividend		(36,000)	
nterest paid on Long term Borrowings		(35,000)	
Net cash from financing activities		1,14,000	1,14,000

Net increase in cash and cash equivalents	1,20,000
Add : Cash and cash equivalents in the beginning of the period(5)	94,000
Cash and cash equivalents at the end of the period(5)	2,14,000

Notes : (1) Calculation of Net Profit before Tax :

	₹
Profit & Loss Balance on 31st March, 2022	56,000
Less : Profit & Loss Balance on 31st March, 2021	(30,000)
	86,000
Add : Interim Dividend Paid	36,000
Net Profit before Tax	1,22,000

Negative balance of Profit & Loss amounting to ₹30,000 appearing in the Balance Sheet on 31st March, 2021 represents an amount of loss. In the current year, after covering this loss of ₹30,000, the Profit & Loss shows a profit of ₹56,000. It means that net profit during the current year must have been ₹56,000 + ₹30,000 = ₹86,000.

(2)

Dr. **FIXED TANGIBLE ASSETS A/C** *(On Original Cost)* Cr.

Particulars	₹	*Particulars*	₹
To Balance b/d	2,00,000	By Bank (sale)	17,000
To Gain on Sale of Fixed Tangible Assets	5,000	By Accumulated Dep. A/c (Being depreciation on fixed tangible assets sold)	8,000
To Bank A/c (Balancing figure, being purchase)	3,20,000	By Balance c/d	5,00,000
	5,25,000		5,25,000

(3)

Dr. **ACCUMULATED DEPRECIATION A/C** Cr.

Particulars	₹	*Particulars*	₹
To Fixed Tangible Assets A/c (being the transfer of depreciation on fixed tangible assets sold)	8,000	By Balance b/d	30,000
To Balance c/d	48,000	By Depreciation A/c (Balancing figure, being current year's depreciation)	26,000
	56,000		56,000

(4)

Dr. **NON-CURRENT INVESTMENTS A/C** Cr.

Particulars	₹	*Particulars*	₹
To Balance b/d	40,000	By Bank A/c (Sale proceeds)	14,000
To Gain on sale of Non-Current Investments	4,000	By Balance c/d	45,000
To Bank A/c (Balancing figure-being purchases)	15,000		
	59,000		59,000

(5) Cash and Cash Equivalents :	2022 (₹)	2021 (₹)
Cash and Bank	1,84,000	44,000
Current Investments (Short-term)	30,000	50,000
	2,14,000	94,000

ILLUSTRATION 40.

From the following Balance Sheets of *X* Ltd., you are required to prepare a Cash Flow Statement :

Particulars	*Note No.*	*31.3.2022*	*31.3.2021*
I. EQUITY AND LIABILITIES :		₹	₹
(1) Shareholder's Funds :			
(*a*) Share Capital		2,00,000	2,00,000
(*b*) Reserve and Surplus		1,55,000	80,000
(2) Current Liabilities :			
(*a*) Trade Payables		1,28,000	1,45,000
(*b*) Short term Provision	1	45,000	35,000
TOTAL		5,28,000	4,60,000
II. ASSETS :			
(1) Non-Current Assets :			
Fixed Assets :			
(*i*) Tangible Assets	2	2,00,000	1,50,000
(*ii*) Intangible Assets	3	33,000	40,000
(2) Current Assets :			
(*a*) Current Investments (Marketable Securities)		15,000	12,000
(*b*) Inventory		2,15,000	1,80,000
(*c*) Trade Receivables		50,000	60,000
(*d*) Cash & Bank		10,000	8,000
(*e*) Other Current Assets	4	5,000	10,000
TOTAL		5,28,000	4,60,000

Notes :	*31.3.2022*	*31.3.2021*
(1) Short term Provision :		
Provision for Taxation	45,000	35,000
(2) Tangible Assets :		
Machinery	2,00,000	1,50,000
(3) Intangible Assets :		
Goodwill	33,000	40,000
(4) Other Current Assets :		
Prepaid Expenses	5,000	10,000

Additional Information :

I. Machinery whose original cost was ₹50,000 was sold for ₹10,000 during the year. Accumulated depreciation on this machinery was ₹26,000.

II. Depreciation on Machinery charged during the year ₹20,000.

III. An Interim Dividend was paid during the year @ 10% on Equity share Capital.

SOLUTION :

CASH FLOW STATEMENT
for the year ended 31st March, 2022

Particulars		₹	₹
A. Cash flows from Operating Activities :			
Net Profit before Tax (Note 1)		1,40,000	
Adjustments for non-cash and non-operating items :			
Add : Depreciation on Machinery	20,000		
Loss on sale of Machinery	14,000		
Goodwill written off	7,000	41,000	
Operating profit before working capital changes		1,81,000	
Add : Decrease in Current Assets :			
Trade Receivable	10,000		
Prepaid Expenses	5,000	15,000	
		1,96,000	
Less : Increase in Current Assets :			
Inventory	35,000		
Less : Decrease in Current Liabilities :			
Trade Payable	17,000	52,000	
		1,44,000	
Payment of Tax (for 2021)		35,000	
Net cash from operating activities		1,09,000	1,09,000
B. Cash flows from Investing Activities :			
Purchase of Machinery(2)		(94,000)	
Sale of Machinery		10,000	
Net cash used in investing activities		(84,000)	(84,000)
C. Cash flows from Financing Activities :			
Interim Dividend paid		(20,000)	
Net Cash used in financing activities			(20,000)
Net increase in cash and cash equivalents			5,000
Add : Cash and cash equivalents in the beginning of the period(3)			20,000
Cash and cash equivalents at the end of the period(3)			25,000

Working Note :

(1) Net Profit before Tax

		₹
	Balance of Reserve & Surplus on 31st March, 2022	1,55,000
	(–) Balance of Reserve & Surplus on 31st March, 2021	80,000
		75,000
Add :	Provision for Taxation for 2022	45,000
	Interim Dividend Paid (10% on ₹2,00,000)	20,000
		1,40,000

(2)

MACHINERY ACCOUNT

(On written down value)

Dr.	₹		Cr. ₹
To Balance b/d	1,50,000	By Bank (Sale)	10,000
To Bank A/c (Balancing figure-being purchase)	94,000	By Loss on Sale	14,000
		By Depreciation	20,000
		By Balance c/d	2,00,000
	2,44,000		2,44,000

(3) Cash and Cash Equivalents :

	31-3-2022 (₹)	31-3-2021 (₹)
Cash and Bank	10,000	8,000
Marketable Securities	15,000	12,000
	25,000	20,000

ILLUSTRATION 41.

Following are the Balance Sheets of Sewak Ltd. as at 31.3.2022 and 31.3.2021 :

Particulars	*Note No.*	*31.3.2022* ₹	*31.3.2021* ₹
I. EQUITY AND LIABILITIES :			
(1) Shareholder's Funds :			
(*a*) Share Capital		7,00,000	4,00,000
(*b*) Reserve & Surplus	1	(3,35,000)	(50,000)
(2) Non-Current Liabilities :			
Long-term Borrowings	2	4,00,000	2,00,000
(3) Current Liabilities			
(*a*) Short term Borrowings	3	22,000	30,000
(*b*) Trade Payables		1,28,000	80,000
(*c*) Other Current Liabilities	4	20,000	10,000
TOTAL		9,35,000	6,70,000
II. ASSETS :			
(1) Non-Current Assets :			
(*a*) Fixed Assets		5,00,000	3,00,000
(*b*) Non-Current Investments		1,40,000	2,00,000
(2) Current Assets :			
(*a*) Inventory		1,00,000	50,000
(*b*) Trade Receivables		1,70,000	1,00,000
(*c*) Cash & Bank Balances		25,000	20,000
TOTAL		9,35,000	6,70,000

Notes : (1) Reserve & Surplus :	31.3.2022 (₹)	31.3.2021 (₹)
Profit & Loss Balance	(3,35,000)	(50,000)
(2) Long-term Borrowings :		
9% Debentures	4,00,000	2,00,000

(3) Short -term Borrowings : Cash Credit	22,000	30,000
(4) Other Current Liabilities : Outstanding Expenses	20,000	10,000

Additional Information :

(1) Included in the fixed assets was a piece of machinery costing ₹70,000 on which depreciation charged was ₹40,000 and it was sold for ₹30,000. During the year ₹1,40,000 depreciation was charged on fixed assets.

(2) Share Issue Expenses of ₹15,000 were incurred and written off from the Statement of Profit and Loss in 2021-22.

Prepare a Cash Flow Statement.

SOLUTION :

CASH-FLOW STATEMENT

for the year ended 31st March, 2022

Particulars		₹	₹
A. Cash Flows from Operating Activities			
Net Loss for Current year (Note 1)		(2,85,000)	
Adjustments for non-cash and non-operating items :			
Add : Depreciation on Fixed Tangible Assets		1,40,000	
Interest on Long-term Borrowings (Debentures) (9% on 2,00,000)		18,000	
Share Issue Expenses Written off		15,000	
Operating Loss before Working Capital Changes		(1,12,000)	
Add : Increase in Current Liabilities :			
Trade Payables	48,000		
Outstanding Expenses	10,000	58,000	
		(54,000)	
Less : Increase in Current Assets			
Inventory	50,000		
Trade Receivables	70,000	(1,20,000)	
Net cash used in Operating Activities		(1,74,000)	(1,74,000)
B. Cash flows from Investing Activities :			
Sale of Fixed Tangible Assets (Machinery)		30,000	
Purchase of Fixed Tangible Assets (Note 3)		(3,70,000)	
Sale of Non-Current Investments		60,000	
Net cash used in Investing Activities		(2,80,000)	(2,80,000)
C. Cash flows from Financing Activities :			
Proceeds from Issue of Share Capital		3,00,000	
Share Issue Expenses		(15,000)	
Proceeds from Issue of Long-term Borrowings (Debentures)		2,00,000	
Interest paid on Long-term Borrowings (Debentures)		(18,000)	
Decrease in Cash Credit		(8,000)	
Net Cash from Financing Activities		4,59,000	4,59,000

	₹	₹
Net Increase in Cash and Cash Equivalents (A + B + C)		5,000
Add : Cash and Cash equivalents in the beginning of the period		20,000
Cash and Cash equivalents at the end of the period		25,000

Notes : (1) Calculation of Net Profit before Tax :

	₹
Profit & Loss Balance on 31st March, 2022	(3,35,000)
Less : Profit & Loss Balance on 31st March, 2021	(50,000)
Net Loss for the year	(2,85,000)

(2) It has been assumed that new debentures amounting to ₹2,00,000 have been issued at the end of the accounting year, *i.e.*, on 31st March, 2022

(3) FIXED TANGIBLE ASSETS ACCOUNT

(on written down value)

Dr. Cr.

Particulars	₹	*Particulars*	₹
To Balance b/d	3,00,000	By Depreciation A/c	1,40,000
To Bank A/c (Balancing figure being purchase)	3,70,000	By Bank A/c (Sale)	30,000
		By Balance c/d	5,00,000
	6,70,000		6,70,000

Schedule III is not applicable in case of Sole Proprietorship or Partnership

ILLUSTRATION 42

Following are the Balance Sheets of Mr. Anil. Prepare a Cash Flow Statement :

Liabilities	*31.3.2017*	*31.3.2018*	*Assets*	*31.3.2017*	*31.3.2018*
	₹	₹		₹	₹
Capital	3,00,000	2,20,000	Fixed Assets	3,00,000	2,50,000
Trade Payables	1,10,000	1,31,000	Inventory	80,000	60,000
Outstanding Expenses	—	16,000	Trade Receivables	40,000	42,000
Bank Overdraft	10,000	—	Bank Balance	—	15,000
	4,20,000	3,67,000		4,20,000	3,67,000

Other Information :

I. There was neither any drawings nor any capital addition during the year.
II. There was neither any purchase nor sale of fixed assets during the year.

SOLUTION :

CASH FLOW STATEMENT

for the year ended 31st March, 2018

	₹	₹
A. Cash flows from Operating Activities		
Net Loss for the year (Note 1)	(80,000)	
Adjustments for non-cash and non-operating items :		
Add : Depreciation on Fixed Assets	50,000	
Operating loss before working capital changes	(30,000)	

Add : Decrease in Current Assets :		
Inventory	20,000	
Increase in Current Liabilities :		
Trade Payables	21,000	
Outstanding Expenses	16,000	
	27,000	
Less : Increase in Current Assets :		
Trade Receivables	2,000	
Net cash from operating activities	25,000	25,000
B. Cash flows from Investing Activities		—
C. Cash flows from Financing Activities		—
Repayment of Bank Overdraft	(10,000)	
Net Cash used in Financing Activities	(10,000)	(10,000)
Net increase in cash and cash equivalents		15,000
Add : Cash and cash equivalents in the beginning of the period		—
Cash and cash equivalents at the end of the period		15,000

Notes :

(1) No information is given in the question about the amount of net profit or net loss incurred during the year. As such, the decrease in proprietor's capital will be treated as net loss:

	₹
Opening Capital	3,00,000
Less : Closing Capital	2,20,000
Net Loss	80,000

(2) Bank Overdraft will be treated as financing activity.

ILLUSTRATION 43.

Prepare Cash Flow Statement on the basis of information given in the Balance Sheets of Relga Ltd. as at 31st March, 2019 and 31st March, 2020 :

Particulars	*Note No.*	*31.3.2019*	*31.3.2020*
I. EQUITY AND LIABILITIES :		₹	₹
1. Shareholder's Funds :			
(*a*) Share Capital		2,00,000	2,50,000
(*b*) Reserve and Surplus	1	50,000	70,000
2. Non-Current Liabilities :			
Long-term Borrowings	2	1,00,000	80,000
3. Current Liabilities :			
(*a*) Trade Payables	3	60,000	1,60,000
(*b*) Other Current Liabilities	4	25,000	20,000
TOTAL		4,35,000	5,80,000
II. ASSETS :			
1. Non-Current Assets :			
(*a*) Fixed Assets :			

(*i*) Tangible Assets	5	1,50,000	2,00,000
(*ii*) Intangible Assets	6	10,000	2,000
(*b*) Long-term Loans and Advances		1,00,000	1,30,000
2. **Current Assets :**			
(*a*) Inventories		70,000	90,000
(*b*) Trade Receivables		40,000	60,000
(*c*) Cash and Cash Equivalents		65,000	98,000
TOTAL		4,35,000	5,80,000

Notes to Accounts :

	31.3.2019	*31.3.2020*
(1) Reserves and Surplus	₹	₹
General Reserve	50,000	70,000
(2) Long-term Borrowings		
12% Debentures	1,00,000	80,000
(3) Trade Payables		
Creditors	40,000	60,000
Bills Payable	20,000	1,00,000
	60,000	1,60,000
(4) Other Current Liabilities		
Outstanding Expenses	25,000	20,000
(5) Tangible Fixed Assets		
Machinery	2,00,000	2,60,000
Less : Provision for Depreciation	(50,000)	(60,000)
	1,50,000	2,00,000
(6) Intangible Fixed Assets		
Goodwill	10,000	2,000

Additional Information :

1. During the year a piece of machinery with a book value of ₹30,000; provision for depreciation on it ₹10,000 was sold at a loss of 50% on book value.
2. Debentures were redeemed on 31st March 2020.

(C.B.S.E. Sample Paper 2020)

SOLUTION :

Cash Flow Statement of Relga Ltd. for the year ended 31st March, 2020
(As per AS-3 revised)

Particulars	*Details*	*Amount*
	₹	₹
A. **Cash Flow from Operating Activities :**		
Net Profit before Tax (₹70,000 – ₹50,000)	20,000	

Add : **Non-Operating and Non-cash Items :**		
Loss on Sale of Machinery	15,000	
Depreciation Charged on Machinery	20,000	
Goodwill amortized	8,000	
Interest on Debentures	12,000	
Operating Profit before Changes in Working Capital	75,000	
Changes in Working Capital :		
Increase in Creditors	20,000	
Increase in Bills Payable	80,000	
Decrease in outstanding expenses	(5,000)	
Increase in inventories	(20,000)	
Increase in trade receivables	(20,000)	
Cash Flow from Operating Activities		1,30,000
B. Cash Flow from Investing Activities :		
Sale of Machinery	15,000	
Purchase of Machinery	(1,00,000)	
Loans advanced	(30,000)	
Net Cash used in Investing Activities		(1,15,000)
C. Cash Flow from Financing Activities		
Issue of Share Capital	50,000	
Debentures Redeemed	(20,000)	
Interest paid on Debentures	(12,000)	
Cash Flow from Financing Activities		18,000
Net Increase in Cash and Cash Equivalents during the year		33,000
Add : Opening Cash and Cash equivalents		65,000
Closing Cash and Cash equivalents		98,000

Dr. MACHINERY A/C Cr

Particulars	*Amount*	*Particulars*	*Amount*
	₹		₹
To Balance b/d	2,00,000	By Bank A/c (Sale)	15,000
To Bank A/c (Balancing Figure being Purchase)	1,00,000	By Loss on Sale of Machinery A/c	15,000
		By Provision for Depreciation A/c	10,000
		By Balance c/d	2,60,000
	3,00,000		3,00,000

Dr. PROVISION FOR DEPRECIATION A/C C

Particulars	*Amount*	*Particulars*	*Amoun*
	₹		₹
To Machinery A/c	10,000	By Balance b/d	50,00
To Balance c/d	60,000	By Depreciation A/c (Balancing Figure, being Current Year's Depreciation	20,00
	70,000		70,00

ILLUSTRATION 44.

Cash used in operating activities of Starline Ltd. for the year ended 31.03.2019 was ₹18,000. The Balance Sheet along with notes to accounts of Starline Ltd. as at 31.3.2019 is given below :

Starline Ltd.
Balance Sheet as at 31st March, 2019

Particulars	*Note No.*	*31-3-2019* ₹	*31-3-2018* ₹
Equity and Liabilities :			
1. Shareholder's Funds			
(*a*) Share Capital		18,00,000	10,00,000
(*b*) Reserves and Surplus	1	50,000	40,000
2. Non-current Liabilities			
Long term borrowings	2	1,00,000	4,00,000
3. Current Liabilities			
Short term provisions	3	2,50,000	3,60,000
TOTAL		22,00,000	18,00,000
Assets :			
1. Non-current Assets			
Fixed Assets			
(*i*) Tangible Assets	4	14,00,000	10,00,000
(*ii*) Intangible Assets	5	1,80,000	70,000
2. Current Assets			
(*a*) Current Investments		30,000	1,90,000
(*b*) Trade Receivables		2,90,000	3,10,000
(*c*) Cash and Cash Equivalents		3,00,000	2,30,000
TOTAL		22,00,000	18,00,000

Notes to Accounts :

Note No.	*Particulars*	*31-3-2019* ₹	*31-3-2018* ₹
1.	**Reserves and Surplus :**		
	Surplus (Balance in Statement of Profit & Loss)	50,000	40,000
2.	**Long term Borrowings :**		
	8% Debentures	1,00,000	4,00,000
3.	**Short-term Provisions :**		
	Provision for Tax	2,50,000	3,60,000
4.	**Tangible Assets :**		
	Plant & Machinery	15,20,000	10,90,000
	Less : Accumulated Depreciation	(1,20,000)	(90,000)
		14,00,000	10,00,000

5.	**Intangible Assets :** Goodwill	1,80,000	70,000

You are given the following additional information :

(*a*) A machinery of the book value of ₹40,000 (depreciation provided thereon ₹12,000) was sold at a loss of ₹6,000.

(*b*) 8% debentures were redeemed on 1st July 2018.

Prepare Cash Flow Statement. (C.B.S.E. 2020, Delhi)

SOLUTION :

Starline Ltd.
CASH FLOW STATEMENT
for the year ended 31st March, 2019

Particulars	₹	₹
(A) **Cash Flow from Operating Activities :**		
Net Cash used in Operating Activities		(18,000)
(B) **Cash Flows from Investing Activities :**		
Sale of Plant & Machinery	34,000	
Purchase of Plant & Machinery	(4,82,000)	
Purchase of Goodwill	(1,10,000)	
Net Cash used in investing activities	(5,58,000)	(5,58,000)
(C) **Cash Flows from Financing Activities :**		
Issue of Share Capital	8,00,000	
Redemption of Debentures	(3,00,000)	
Interest paid on Debentures(2)	(14,000)	
Net Cash from financing activities	4,86,000	4,86,000
Net decrease in Cash and Cash equivalents		(90,000)
Add : Cash and Cash equivalents in the beginning		4,20,000
Cash and Cash equivalents at the end		3,30,000

Working Notes : (1)

Dr. PLANT & MACHINERY ACCOUNT Cr.

Particulars	₹	*Particulars*	₹
To Balance b/d	10,90,000	By Bank A/c	34,000
To Bank A/c (Balancing figure, being purchase)	4,82,000	By Accumulated Dep. A/c	12,000
		By Loss on Sale of Machinery	6,000
		By Balance c/d	15,20,000
	15,72,000		15,72,000

(2) Interest Paid on Debentures :

	₹
On ₹4,00,000 @8% for 3 months	8,000
On ₹1,00,000 @8% for 9 months	6,000
	14,000

(3) Cash and Cash Equivalents :

	31.3.2019	31.3.2018
	₹	₹
Current Investments	30,000	1,90,000
Cash and Cash Equivalents	3,00,000	2,30,000
	3,30,000	4,20,000

ILLUSTRATION 45.

From the following Balance Sheet of Gopal Ltd. and the additional information as at 31st March, 2019, prepare a Cash Flow Statement when cash flows from financing activities is ₹2,32,000.

Gopal Ltd.
BALANCE SHEET
as at 31-3-2019

Particulars	*Note No.*	*31st March 2019 (₹)*	*31st March 2018 (₹)*
I. Equity and Liabilities :			
1. Shareholder's Funds			
(a) Share Capital		10,00,000	8,00,000
(b) Reserve and Surplus	1	4,00,000	(1,00,000)
2. Non-Current Liabilities			
Long term Borrowings	2	9,00,000	9,00,000
3. Current Liabilities			
(a) Short term Borrowings	3	2,40,000	1,00,000
(b) Short term Provisions	4	2,00,000	1,75,000
TOTAL		27,40,000	18,75,000
II. Assets :			
1. Non-Current Assets			
(a) Fixed Assets			
(i) Tangible Assets	5	20,00,000	14,42,000
(ii) Intangible Assets	6	46,000	58,000
(b) Non-Current Investments		1,00,000	45,000
2. Current Assets :			
(a) Current Investments		2,00,000	1,20,000
(b) Inventories	7	2,14,000	90,000
(c) Cash and Cash Equivalents		1,80,000	1,20,000
TOTAL		27,40,000	18,75,000

Notes to Accounts :

Note No.	*Particulars*	*31 March 2019 (₹)*	*31 March 2018 (₹)*
1.	**Reserve and Surplus**		
	Surplus (Balance in Statement of Profit and Loss)	4,00,000	(1,00,000)
2.	**Long Term Borrowings**		
	12% Debentures	9,00,000	9,00,000

3.	**Short Term Borrowings** Bank Overdraft	2,40,000	1,00,000
4.	**Short Term Provisions** Provision for Tax	2,00,000	1,75,000
5.	**Tangible Assets** Machinery *Less* : Accumulated Depreciation	24,00,000 (4,00,000) 20,00,000	16,42,000 (2,00,000) 14,42,000
6.	**Intangible Assets** Goodwill	46,000	58,000
7.	**Inventories** Stock in Trade	2,14,000	90,000

Additional Information :

Tax ₹1,50,000 was paid during the year. *(C.B.S.E. 2020, Punjab)*

SOLUTION :

CASH FLOW STATEMENT OF GOPAL LTD.
for the year ended 31st March 2019

Particulars	*Details* ₹	*Amount* ₹
CASH FLOWS FROM OPERATING ACTIVITIES		
Net Profit before Tax(1)	6,75,000	
Adjustment for Non Cash and Non Operating Items :		
Add : Interest on Debentures	1,08,000	
Depreciation	2,00,000	
Goodwill Written Off	12,000	
Operating Profit before Working Capital Changes	9,95,000	
Less : Increase in Inventory	(1,24,000)	
Cash from Operations	8,71,000	
Less : Tax Paid	(1,50,000)	
Cash Inflows from Operating Activities		7,21,000
CASH FLOWS FROM INVESTING ACTIVITIES		
Purchase of Plant and Machinery	(7,58,000)	
Purchase of Investments	(55,000)	
Cash used in Investing Activities		(8,13,000)
CASH FLOWS FROM FINANCING ACTIVITIES		
Cash Inflows from Financing Activities		2,32,000
Net increase in Cash and Cash Equivalents		1,40,000
Add : Opening Balance of Cash and Cash Equivalents		2,40,000
Closing Balance of Cash and Cash Equivalents		3,80,000

Working Notes :

(1) Calculation of Net Profit before Tax :

	₹
Balance in Statement of P & L on 31.3.2018	(1,00,000)
Balance in Statement of P & L on 31.3.2019	4,00,000
	5,00,000
Add : Provision for Tax (Refer Note 2)	1,75,000
	6,75,000

(2)

Dr. PROVISION FOR TAX A/C Cr.

Particulars	*Amount*	*Particulars*	*Amount*
	₹		₹
To Bank A/c (Given)	1,50,000	By Balance b/d	1,75,000
To Balance c/d	2,00,000	By Statement of P & L — (Balancing Figure, being Provision made)	1,75,000
	3,50,000		3,50,000

(3) **Cash and Cash Equivalents :**

	31.3.2019	*31.3.2018*
	₹	₹
Current Investments	2,00,000	1,20,000
Cash and Cash Equivalents	1,80,000	1,20,000
	3,80,000	2,40,000

ILLUSTRATION 46.

Calculate Cash from operating activities from the following :

	31st March, 2022	*31st March, 2021*
	₹	₹
Surplus i.e. Balance in the Statement of Profit & Loss	80,000	1,00,000
Trade Receivables	2,50,000	2,40,000
Goodwill	15,000	20,000
Outstanding Expenses	8,000	–
General Reserve	80,000	50,000
Provision for Depreciation on Plant	1,00,000	82,000
Prepaid Expenses	—	6,000
Trade Payables	84,000	60,000

Additional Information :

(*i*) Plant costing ₹60,000 having book value of ₹36,000 was sold for ₹40,000 during the year.

(*ii*) Income Tax paid during the year ₹30,000.

(*iii*) Interim Dividend paid during the year ₹18,000.

SOLUTION :

CALCULATION OF CASH FROM OPERATING ACTIVITIES

for the year ended 31st March, 2022

	₹	₹
Net Profit before Tax (Note 1)		58,000
Adjustments for non-cash and non-operating items :		
Add : Goodwill written off	5,000	
Depreciation on Fixed Tangible Assets (Plant)(3)	42,000	47,000
		1,05,000
Less : Profit on Sale of Fixed Tangible Assets (Plant)(2)		4,000
Operating profit before working capital changes		1,01,000
Add : Decrease in Current Assets :		
Prepaid Expenses	6,000	
Increase in Current Liabilities :		
Outstanding Expenses	8,000	
Trade Payables	24,000	38,000
		1,39,000
Less : Increase in Current Assets :		
Trade Receivables		10,000
Cash flow from operating activities before tax		1,29,000
Less : Income Tax Paid		30,000
Cash flow from operating activities after tax		99,000

Working Notes :

(1) Calculation of Net Profit before Tax :

		₹
Closing Surplus, *i.e.*, Balance in Statement of Profit and Loss		80,000
Opening Surplus, *i.e.*, Balance in Statement of Profit and Loss		1,00,000
Net Loss during the year		(20,000)
Add : Tax paid	30,000	
Interim Dividend paid	18,000	
Transfer to General Reserve	30,000	78,000
Net Profit before Tax		58,000

(2)

PLANT SOLD ACCOUNT

(On Original Cost)

Dr. Cr.

Particulars	₹	Particulars	₹
To Balance b/d	60,000	By Bank A/c	40,000
To Gain on Sale of Plant	4,000	By Provision for Depreciation A/c (Being the Depreciation on Plant Sold)	24,000
	64,000		64,000

(3)

PROVISION FOR DEPRECIATION ON PLANT ACCOUNT

Dr. Cr.

Particulars	₹	Particulars	₹
To Plant A/c (Being the transfer of Depreciation on Plant Sold)	24,000	By Balance b/d	82,000
To Balance c/d	1,00,000	By Depreciation A/c (Balancing Figure — Being the Current Year's Depreciation)	42,000
	1,24,000		1,24,000

ILLUSTRATION 47.

From the following information, prepare a Cash Flow Statement :

	₹
Opening Cash Balance	15,000
Closing Cash Balance	17,000
Decrease in Inventory	8,000
Increase in Bills Payable	12,000
Sale of Fixed Assets	30,000
Repayment of Long Term Loan	50,000
Net Profit for the Year	2,000

SOLUTION :

CASH FLOW STATEMENT

for the year ended ....

Particulars		₹	₹
A. Cash flows from Operating Activities :			
Net profit before taxation		2,000	
Add : Decrease in Current Assets :			
Inventory	8,000		
Add : Increase in Current Liabilities :			
Bills Payable	12,000	20,000	
Net cash from operating activities		22,000	22,000
B. Cash flows from Investing Activities :			
Sale of fixed assets		30,000	
Net Cash from investing activities			30,000
C. Cash flows from Financing Activities :			
Repayment of Long-term Loan		(50,000)	
Net cash used in financing activities			(50,000)
Net increase in cash and cash equivalents			2,000
Add : Cash and cash equivalents in the beginning of the period			15,000
Cash and cash equivalents at the end of the period			17,000

ILLUSTRATION 48.

From the following Balance Sheets of XYL limited, prepare Cash Flow Statement:

Particulars	*Note No.*	*31.3.2018*	*31.3.2017*
		₹	₹
I. EQUITY AND LIABILITIES :			
(1) Shareholder's Funds :			
(*a*) Share Capital		5,00,000	4,50,000
(*b*) Reserve and Surplus	1	1,18,000	70,000
(2) Current Liabilities			
(*a*) Trade Payables		1,49,000	1,17,000
(*b*) Short term Provisions (Provision for Tax)		50,000	40,000
TOTAL		8,17,000	6,77,000
II. ASSETS :			
(1) Non-Current Assets :			
(*a*) Fixed Assets			
(*i*) Tangible Assets	2	3,70,000	2,80,000
(*ii*) Intangible Assets	3	90,000	1,15,000
(2) Current Assets :			
(*a*) Inventory		1,09,000	77,000
(*b*) Trade Receivables		2,30,000	1,80,000
(*c*) Cash & Bank Balances		18,000	25,000
TOTAL		8,17,000	6,77,000

Notes :	*31.3.2018*	*31.3.2017*
(1) Reserve & Surplus :	₹	₹
General Reserve	70,000	40,000
Profit & Loss Balance	48,000	30,000
	1,18,000	70,000
(2) Tangible Assets :		
Land and Building	1,70,000	2,00,000
Plant	2,00,000	80,000
	3,70,000	2,80,000
(3) Intangible Assets :		
Goodwill	90,000	1,15,000

Additional Information :

(*a*) Contingent Liability	*31.3.2018*	*31.3.2017*
Proposed Dividend (₹)	50,000	42,000

(*b*) Depreciation of ₹10,000 and ₹20,000 has been charged on plant, land and buildings respectively.

(*c*) An interim dividend of ₹20,000 has been paid.

(*d*) Income tax of ₹35,000 has been paid.

(*e*) Rent Received during the year ₹10,000.

SOLUTION : CASH FLOW STATEMENT OF XYL LIMITED
for the year ended 31st March 2018

Particulars	₹	₹
A. Cash Flows from Operating Activities :		
Profit before Tax (Working Note 1)	1,55,000	

Adjustments for non-cash and non-operating items :			
Add : Depreciation on Plant	10,000		
Depreciation on Land and Building	20,000		
Goodwill written off	25,000	55,000	
		2,10,000	
Less : Rent Received		10,000	
Operating profit before working capital changes		2,00,000	
Add : Increase in Current Liabilities :			
Trade Payables		32,000	
		2,32,000	
Less : Increase in Current Assets :			
Inventory	32,000		
Trade Receivables	50,000	(82,000)	
Cash generated from operating activities		1,50,000	
Less : Income Tax paid		(35,000)	
Net Cash from operating activities		1,15,000	1,15,000
B. Cash Flows from Investing Activities :			
Sale of Land and Building(2)		10,000	
Purchase of Plant(3)		(1,30,000)	
Rent Received		10,000	
Net Cash used in investing activities		(1,10,000)	(1,10,000)
C. Cash Flows from Financing Activities :			
Issue of share capital		50,000	
Payment of proposed dividend (for 2017)		(42,000)	
Interim dividend paid		(20,000)	
Net Cash used in financing activities		(12,000)	(12,000)
Net Decrease in cash and cash equivalents			(7,000)
Add : Cash and cash equivalents in the beginning of the period			25,000
Cash and cash equivalents at the end of the period			18,000

Working Notes :

		₹
(1) Profit before Tax :		
	Profit & Loss Balance on 31st March, 2018	48,000
Less :	Profit & Loss Balance on 31st March, 2017	30,000
		18,000
Add :	Proposed Dividend for 2017	42,000
	Interim Dividend paid	20,000
	Transfer to General Reserve	30,000
	Provision for Taxation(4)	45,000
		1,55,000

There will be no effect of proposed dividend of 2018.

(2)

Dr. LAND AND BUILDING ACCOUNT Cr.

Particulars	₹	*Particulars*	₹
To Balance b/d	2,00,000	By Depreciation A/c	20,000
		By Bank A/c (Balancing figure, being sales)	10,000
		By Balance c/d (Given)	1,70,000
	2,00,000		2,00,000

(3)

Dr. PLANT ACCOUNT Cr.

Particulars	₹	*Particulars*	₹
To Balance b/d	80,000	By Depreciation A/c	10,000
To Bank A/c (Balancing figure, being purchase)	1,30,000	By Balance c/d (Given)	2,00,000
	2,10,000		2,10,000

(4)

Dr. PROVISION FOR TAX ACCOUNT Cr.

Particulars	₹	*Particulars*	₹
To Bank A/c (Payment made) (Given)	35,000	By Balance b/d (Given)	40,000
To Balance c/d (Given)	50,000	By Statement of P & L (Balancing figure, being provision made in 2018)	45,000
	85,000		85,000

(5) Rent received is deducted from Profits because it is related to investment in property. It will be shown as inflow of cash under Investing Activity.

ILLUSTRATION 49.

From the following information, prepare Cash Flow Statement :

BALANCE SHEET

as at 31.3.2022 and 31.3.2021

Particulars	*Note No.*	*31.3.2022*	*31.3.2021*
I. EQUITY AND LIABILITIES :		₹	₹
(1) Shareholder's Funds :			
(*a*) Share Capital		1,00,000	80,000
(*b*) Reserve and Surplus	1	6,400	6,000
(2) Non-Current Liabilities			
Long-term Borrowings	2	14,000	12,000
(3) Current Liabilities			
(*a*) Short-term Borrowings	3	13,600	25,000
(*b*) Trade Payables		31,600	34,000

(c) Short term Provisions (Provision for Tax)		8,400	6,000
(d) Other Current Liabilities	4	2,000	—
TOTAL		1,76,000	1,63,000
II. ASSETS :			
(1) **Non-Current Assets :**			
Fixed Assets	5	50,000	60,000
(2) **Current Assets :**			
(a) Inventories		70,000	60,000
(b) Trade Receivables		48,000	40,000
(c) Cash & Bank Balances		7,000	2,400
(d) Prepaid Expenses		1,000	600
TOTAL		1,76,000	1,63,000

Notes :	*31.3.2022*	*31.3.2021*
	₹	₹
(1) Reserve & Surplus :		
General Reserve	4,000	4,000
Profit & Loss Balance	2,400	2,000
	6,400	6,000
(2) Long-term Borrowings :		
15% Debentures	14,000	12,000
(3) Short-term Borrowings :		
Cash Credit	13,600	25,000
(4) Other Current Liabilities :		
Dividend Payable	2,000	—
(5) Fixed Assets	80,000	82,000
Less : Accumulated Depreciation	30,000	22,000
	50,000	60,000

Additional Information :

	31.3.2022	*31.3.2021*
(a) Contingent Liability : Proposed Dividend (₹)	11,600	10,000

(b) Provision for tax made ₹9,400.

(c) Fixed assets sold for ₹10,000, their cost ₹20,000 and accumulated depreciation till date of sale is ₹6,000.

(d) An interim dividend paid during the year ₹9,000.

SOLUTION :

CASH FLOW STATEMENT
for the year ended 31st March, 2022

		₹	₹
A. Cash Flows from Operating Activities :			
Net profit before Tax (Note 1)		28,800	
Adjustments for non-cash and non-operating items :			
Add : Depreciation(4)	14,000		

Loss on sale of fixed assets	4,000		
Interest on Debentures	1,800	19,800	
Operating profit before working capital changes		48,600	
Less : Increase in Current Assets :			
Inventories	10,000		
Trade Receivables	8,000		
Prepaid Expenses	400		
Decrease in Current Liabilities :			
Trade Payables	2,400	(20,800)	
Cash generated from operating activities		27,800	
Less : Income Tax paid(5)		(7,000)	
Net cash from Operating Activities		20,800	20,800
B. Cash Flows from Investing Activities :			
Sale of fixed assets		10,000	
Purchase of Fixed Assets(3)		(18,000)	
Net Cash used in investing activities		(8,000)	(8,000)
C. Cash Flows from Financing Activities :			
Issue of share capital		20,000	
Issue of Debentures		2,000	
Interest on Debentures		(1,800)	
Decrease in Cash Credit(6)		(11,400)	
Payment of proposed dividend (for 2021) (₹10,000 – Dividend Payable ₹2,000)(7)		(8,000)	
Interim dividend paid		(9,000)	
Net Cash used in financing activities		(8,200)	(8,200)
Net Increase in cash and cash equivalents			4,600
Add : Cash and cash equivalents in the beginning of the period			2,400
Cash and cash equivalents at the end of the period			7,000

Notes : (1) Calculation of Net Profit before Tax :

		₹
	Profit & Loss Balance on 31st March, 2022	2,400
Less :	Profit & Loss Balance on 31st March, 2021	2,000
		400
Add :	Proposed Dividend for Previous year	10,000
	Interim Dividend Paid	9,000
	Provision for Tax made during the Current year	9,400
		28,800

(2) It is assumed that new debentures have been issued at the end of current accounting period. Hence interest on debentures is 15% on ₹12,000.

(3)

Dr. FIXED ASSETS ACCOUNT (On Original Cost) Cr.

Particulars	₹	*Particulars*	₹
To Balance b/d	82,000	By Bank (Sale)	10,000

To Bank (Balancing figure, being purchase)	18,000	By Accumulated Depreciation A/c (Being depreciation on fixed assets sold)	6,000
		By Loss on sale of fixed assets	4,000
		By Balance c/d	80,000
	1,00,000		1,00,000

(4)

Dr. **ACCUMULATED DEPRECIATION ACCOUNT** Cr.

Particulars	₹	*Particulars*	₹
To Fixed Assets A/c (transfer of depreciation on fixed assets sold)	6,000	By Balance b/d	22,000
To Balance c/d	30,000	By Depreciation A/c (Balancing figure, being current year's depreciation)	14,000
	36,000		36,000

(5)

Dr. **PROVISION FOR TAX ACCOUNT** Cr.

Particulars	₹	*Particulars*	₹
To Bank (balancing figure, being payment made)	7,000	By Balance b/d (Given)	6,000
To Balance c/d (Given)	8,400	By Statement of P & L (Provision made in 2018 (Given)	9,400
	15,400		15,400

(6) Decrease in Cash Credit will be treated as financing activity.

(7) Dividend payable will be deducted from last year's 'Proposed Dividend' to ascertain the actual payment for dividend.

ILLUSTRATION 52.

You are required to prepare a Cash-Flow Statement (as per AS-3) for the year 2021-22 from the following Balance Sheets :

Balance Sheets of Janaki India Ltd.
as at 31st March, 2022 and 31st March, 2021

Particulars	*Note No.*	*31.03.2022* ₹	*31.03.2021* ₹
I. EQUITY AND LIABILITIES			
1. Shareholders' Funds			
(*a*) Share Capital (Equity Share Capital)		3,00,000	2,00,000
(*b*) Reserves and Surplus (Statement of P/L)		1,20,000	70,000
2. Non-Current Liabilities			
(*a*) Long Term Borrowings (8% Debentures)		1,50,000	1,20,000
3. Current Liabilities			
(*a*) Short Term Borrowings (Bank Overdraft)		19,000	5,000

(b) Trade Payables (Creditors)		81,000	80,000
(c) Short Term Provisions	1	82,000	61,600
TOTAL		7,52,000	5,36,600
II. ASSETS			
1. Non-Current Assets			
(a) Fixed Assets			
Tangible	2	2,04,200	1,83,000
(b) Non-Current Investments		1,30,000	1,20,000
2. Current Assets			
(a) Inventories		1,41,500	1,25,000
(b) Trade Receivables		64,600	64,500
(c) Cash and Bank Balances		2,11,700	44,100
TOTAL		7,52,000	5,36,600

Notes to Accounts :

Particulars	*31.03.2022* ₹	*31.03.2021* ₹
1. Short term Provisions		
Provision for Taxation	80,000	60,000
Provision for Doubtful Debts	2,000	1,600
	82,000	61,600
2. Fixed Assets (Tangible)		
Plant and Machinery	2,43,000	2,23,000
Less : Accumulated Depreciation	(38,800)	(40,000)
	2,04,200	1,83,000

Additional Information :

During the year 2021-22 :

(*i*) A part of the machine was sold for ₹21,000 at a profit of ₹4,000.

(*ii*) The company charged ₹3,000 as depreciation on its Plant and Machinery.

(*iii*) New Debentures were issued on 31st March, 2022, at a discount of 10%.

(*iv*) Interest of ₹9,600 was paid on Debentures.

(*v*) Contingent Liability :	*31.3.2022*	*31.3.2021*
Proposed Dividend	25%	30%

(I.S.C. 2016, Modified)

SOLUTION :

Janaki India Ltd.

CASH FLOW STATEMENT

for the year ended 31st March, 2022

Particulars	₹	₹
A. Cash Flows from Operating Activities :		
Net Profit before Tax (Note 1)	1,90,000	

Adjustments for non-cash and non-operating items			
Add : Depreciation on Plant & Machinery		3,000	
Provision for Doubtful Debts		400	
Discount on Issue of Debentures Written off		3,000	
Interest paid on Long term Borrowings (Debentures)		9,600	
		2,06,000	
Less : Gain on Sale of Machine		4,000	
Operating Profit before Working Capital Changes		2,02,000	
Add : Increase in Current Liabilities			
Trade Payables		1,000	
		2,03,000	
Less : Increase in Current Assets			
Inventory	16,500		
Trade Receivables	100	(16,600)	
Cash Generated from Operating Activities		1,86,400	
Less : Tax Paid (for 2021)		60,000	
Net Cash from Operating Activities		1,26,400	1,26,400
B. Cash Flows from Investing Activities :			
Purchase of Plant & Machinery (Note 2)		(41,200)	
Sale of Machinery		21,000	
Purchase of Non-Current Investments		(10,000)	
Net Cash used in Investing Activities		(30,200)	(30,200)
C. Cash Flows from Financing Activities :			
Proceeds from Issue of Share Capital		1,00,000	
Proceeds from Long term Borrowings (Debentures)		27,000	
Proceeds from Short term Borrowings (Bank Overdraft)		14,000	
Interest paid on Long-term Borrowings (Debentures)		(9,600)	
Proposed Dividend Paid (for 2021)		(60,000)	
Net Cash from Financing Activities		71,400	71,400
Net Increase in Cash and Cash Equivalents			1,67,600
Add : Cash and Cash Equivalents at the beginning			44,100
Cash and Cash Equivalents at the end			2,11,700

Working Notes :

(1) Calculation of Net Profit before Tax :

		₹
	Balance of Statement of Profit & Loss on 31st March, 2022	1,20,000
Less :	Balance of Statement of Profit & Loss on 31st March, 2021	70,000
		50,000
Add :	Provision for Tax (for 2022)	80,000
	Proposed Dividend (for 2021) (30% of ₹2,00,000)	60,000
		1,90,000

(2)

Dr. PLANT AND MACHINERY ACCOUNT (On Original Cost) Cr.

Particulars	₹	Particulars	₹
To Balance b/d	2,23,000	By Bank A/c (Sale)	[illegible]
To Gain on sale of machinery	4,000	By Accumulated Depreciation A/c (Being depreciation on machinery sold)*	4,200
To Bank A/c (Balancing figure, being purchase)	41,200	By Balance c/d	[illegible]
	2,68,200		[illegible]

(3)

Dr. ACCUMULATED DEPRECIATION ACCOUNT Cr.

Particulars	₹	Particulars	₹
To Plant & Machinery A/c (Balancing figure, being the depreciation on machinery sold)*	4,200	By Balance b/d	[illegible]
To Balance c/d	38,800	By Depreciation A/c (Current Year's depreciation)	[illegible]
	43,000		[illegible]

*Balancing figure of Accumulated Depreciation Account ₹4,200, is the depreciation on machinery sold. It will be transferred to the credit side of Plant & Machinery Account.

ILLUSTRATION 51.

From the following Balance Sheets of Sunlight Ltd. prepare a Cash-Flow Statement for the year ended 31st March 2019.

Particulars	Note No.	31.3.2019	31.3.2018
I. EQUITY AND LIABILITIES :		₹	₹
(1) Shareholder's Funds :			
(*a*) Share Capital		4,50,000	[illegible]
(*b*) Reserve & Surplus	1	2,06,000	[illegible]
(2) Non-Current Liabilities :			
Long-term Borrowings	2	78,000	[illegible]
(3) Current Liabilities :			
(*a*) Short term Borrowings	3	50,000	[illegible]
(*b*) Trade Payables	4	41,000	[illegible]
TOTAL		[illegible]	[illegible]
II. ASSETS :			
(1) Non-Current Assets :			
(*a*) Fixed Assets		[illegible]	[illegible]
(*b*) Non-Current Investments	5	[illegible]	[illegible]
(2) Current Assets :			
(*a*) Inventory		[illegible]	[illegible]

(b) Trade Receivables		2,44,000	1,52,000
(c) Cash and Bank Balances		30,000	34,000
TOTAL		8,24,000	6,66,000

Notes :

	31.3.2019	31.3.2018
(1) Reserve & Surplus :	₹	₹
General Reserve	1,40,000	1,00,000
Profit & Loss Balance	66,000	74,000
	2,06,000	1,74,000
(2) Long-term Borrowings : 10% Public Deposits	75,000	50,000
(3) Short-term Borrowings : Cash Credit	50,000	20,000
(4) Trade Payables :		
Sundry Creditors	35,000	28,000
Bills Payables	8,000	14,000
	43,000	42,000

(5) Rate of Interest on Investments : 12% p.a.

Additional Information :

(i) A new machinery was purchased for ₹50,000 during the year.

(ii) Non-Current Investments costing ₹25,000 were sold at a loss of ₹3,000 at the end of the year.

SOLUTION :

CASH-FLOW STATEMENT

for the year ended 31st March, 2019

Particulars		₹	₹
A. Cash Flows from Operating Activities			
Net profit before Tax (Note 1)		32,000	
Adjustments for non-cash and non-operating items :			
Add : Depreciation on Machinery$^{(4)}$	15,000		
Loss on sale of Non-Current Investments	3,000		
Interest on Public Deposits (10% on 50,000)$^{(2)}$	5,000	23,000	
		55,000	
Less : Interest on Non-Current Investments (12% on 25,000)$^{(3)}$		(3,000)	
Operating profit before working capital changes		52,000	
Add : Increase in Current Liabilities			
Sundry Creditors		7,000	
		59,000	
Less : Decrease in Current Liabilities			
Bills Payables	6,000		
Less : Increase in Current Assets :			
Inventory	20,000		
Trade Receivables	92,000	1,18,000	

Net cash used in operating activities	(59,000)	(59,000)
B. Cash flows from Investing Activities :		
Purchase of machinery	(50,000)	
Purchase of Non-Current Investments(5)	(40,000)	
Sale of Non-Current Investments	22,000	
Interest on Non-Current Investments	3,000	
Net cash used in investing activities	(65,000)	(65,000)
C. Cash flows from Financing Activities :		
Issue of Share Capital	70,000	
Receipts from Public Deposits	25,000	
Interest paid on Public Deposits	(5,000)	
Increase in Cash Credit	30,000	
Net cash flow from financing activities	1,20,000	1,20,000
Net decrease in Cash and Cash Equivalents		(4,000)
Add : Cash and Cash equivalents in the beginning of the period		34,000
Cash and Cash equivalents at the end of the period		30,000

Notes : (1) Calculation of Net Profit before Tax :

	₹
Profit & Loss Balance on 31st March, 2019	66,000
Less : Profit & Loss Balance on 31st March, 2018	74,000
	(8,000)
Add : Transfer to General Reserve	40,000
Net Profit before Tax	32,000

(2) It has been assumed that new public deposits amounting to ₹25,000 have been accepted at the end of the accounting year, *i.e.*, on 31st March, 2019.

(3) It has been assumed that investments have been purchased at the end of the accounting year.

(4)

Dr. FIXED ASSETS ACCOUNT Cr.

Particulars	₹	*Particulars*	₹
To Balance b/d	1,75,000	By Depreciation A/c (Balancing figure, being current year's Depreciation)	15,000
To Bank A/c (Purchase of Machinery)	50,000	By Balance c/d (Given)	2,10,000
	2,25,000		2,25,000

(5)

Dr. NON-CURRENT INVESTMENTS ACCOUNT Cr.

Particulars	₹	*Particulars*	₹
To Balance b/d	25,000	By Bank A/c (Sale proceeds)	22,000
To Bank A/c (Balancing figure being purchases)	40,000	By Loss on Sale	3,000
		By Balance c/d	40,000
	65,000		65,000

(6) Interest received is a receipt from non-operating activities being related to Investments. Hence, it is deducted from Profits and is shown as Inflow of Cash under Investing Activities.

ILLUSTRATION 52.

From the following Balance Sheets of Humility Ltd., prepare its Cash Flow Statement for the year 2017-18 (as per AS-3) :

Particulars	*Note No.*	*31.3.2018*	*31.3.2017*
I. EQUITY AND LIABILITIES :		₹	₹
(1) **Shareholder's Funds :**			
(*a*) Share Capital		33,00,000	32,00,000
(*b*) Reserve & Surplus	1	5,00,000	4,00,000
(2) **Non-Current Liabilities :**			
Long-term Borrowings	2	16,00,000	15,00,000
(3) **Current Liabilities**			
(*a*) Trade Payables		3,20,000	5,13,000
(*b*) Short-term Provision (Provision for Tax)		30,000	27,000
TOTAL		57,50,000	56,40,000
II. ASSETS :			
(1) **Non-Current Assets :**			
(*a*) Fixed Assets :			
(*i*) Tangible	3	39,50,000	34,60,000
(*ii*) Intangible	4	50,000	40,000
(*b*) Non-current Investments		6,00,000	6,00,000
(2) **Current Assets :**			
(*a*) Current Investments	5	10,000	30,000
(*b*) Trade Receivables		50,000	40,000
(*c*) Inventories		6,00,000	8,00,000
(*d*) Cash & Bank		4,90,000	6,70,000
TOTAL		57,50,000	56,40,000

Notes to Accounts :

	31.3.2018	*31.3.2017*
(1) Reserve & Surplus :	₹	₹
General Reserve	3,50,000	2,80,000
Statement of P & L	1,50,000	1,20,000
	5,00,000	4,00,000
(2) Long-term Borrowings : 10% Debentures	16,00,000	15,00,000
(3) Tangible Assets : Plant & Machinery	39,50,000	34,60,000
(4) Intangible Assets : Goodwill	50,000	40,000
(5) Current Investments : Marketable Securities	10,000	30,000

Additional Information :

(*i*) The debentures were issued on 1.4.2017.

(*ii*) Machinery costing ₹70,000 (accumulated depreciation thereon ₹10,000) was sold for ₹45,000.

(*iii*) Machinery costing ₹8,00,000 was purchased during the year.

(*iv*) Interim dividend of ₹11,000 was paid during the year.

(*v*) Proposed Dividend for the year ended 31st March, 2018 was ₹20,000 and for the year ended 31st March 2017, was ₹13,000.

SOLUTION :

CASH FLOW STATEMENT

for the year ended 31st March, 2018

Particulars		₹	₹
A. Cash Flows from Operating Activities :			
Net profit before Tax (Note 1)		1,54,000	
Adjustments for non-cash and non-operating items :			
Add : Loss on Sale of Machinery		15,000	
Current year's Depreciation on Plant and Machinery (Note 2)		2,50,000	
Interest on Debentures		1,60,000	
Operating Profit before Working Capital Changes		5,79,000	
Add : Decrease in Current Assets :			
Inventory		2,00,000	
		7,79,000	
Less : Increase in Current Assets :			
Trade Receivables	10,000		
Decrease in Current Liabilities :			
Trade Payables	1,93,000	2,03,000	
		5,76,000	
Less : Payment of Tax		27,000	
Net Cash from Operating Activities		5,49,000	5,49,000
B. Cash Flows from Investing Activities :			
Purchase of Machinery		(8,00,000)	
Purchase of Goodwill		(10,000)	
Sale of Machinery		45,000	
Net Cash used in Investing Activities		(7,65,000)	(7,65,000)
C. Cash Flows from Financing Activities :			
Proceeds from Issue of Share Capital		1,00,000	
Proceeds from Issue of Debentures		1,00,000	
Payment of Interim Dividend		(11,000)	
Payment of Proposed Dividend of last year		(13,000)	
Payment of Interest on Debentures		(1,60,000)	
Net Cash flows from Financing Activities		16,000	16,000
Net Decrease in Cash and Cash Equivalents			(2,00,000)

Add : Cash and Cash Equivalents in the beginning of the period(3)		7,00,000
Cash and cash equivalents at the end of the period		5,00,000

Notes : (1) Calculation of Net Profit before Tax :

	₹
Profit & Loss Balance on 31st March, 2018	1,50,000
Less : Profit & Loss Balance on 31st March, 2017	1,20,000
	30,000
Add : Interim Dividend Paid	11,000
Proposed Dividend for Previous year	13,000
Provision for Taxation for Current year	30,000
Transfer to General Reserve	70,000
	1,54,000

(2)

Dr. TANGIBLE ASSETS ACCOUNT Cr.

Particulars	₹	*Particulars*	₹
To Balance b/d	34,60,000	By Bank (Sale)	45,000
To Bank (Purchase)	8,00,000	By Loss on Sale	15,000
		By Depreciation (balancing fig.)	2,50,000
		By Balance c/d	39,50,000
	42,60,000		42,60,000

(3) Cash & Cash Equivalents :

	31.3.2018	*31.3.2017*
	₹	₹
Cash & Bank	4,90,000	6,70,000
Marketable Securities	10,000	30,000
	5,00,000	7,00,000

ILLUSTRATION 53.

From the following Balance Sheets of Diamond Limited as on 31st March, 2013, and 31st March, 2014, prepare a Cash Flow Statement (as per Accounting Standard 3).

Particulars	*Note No.*	*31st March, 2014*	*31st March, 2013*
		₹	₹
I. EQUITY AND LIABILITIES :			
(*i*) **Shareholder's Funds**			
(*a*) Share Capital	1	4,00,000	3,40,000
(*b*) Reserves and Surplus	2	1,60,000	1,20,000
(*ii*) **Non-Current Liabilities**			
Long Term Borrowings	3	3,50,000	2,60,000
(*iii*) **Current Liabilities**			
(*a*) Trade Payables	4	55,000	30,000
(*b*) Other Current Liabilities	5	2,000	5,000
TOTAL		9,67,000	7,55,000

II. ASSETS :			
1. **Non-Current Assets**			
Fixed Assets (Tangible)	6	6,00,000	4,80,000
2. **Current Assets**			
(*a*) Inventories		73,000	50,000
(*b*) Trade Receivables	7	1,55,000	1,30,000
(*c*) Cash and Bank Balances	8	1,39,000	95,000
TOTAL		9,67,000	7,55,000

Notes to Accounts :

Particulars	*31st March, 2014* ₹	*31st March, 2013* ₹
1. **Share Capital**		
Equity Share Capital	4,00,000	3,40,000
2. **Reserves and Surplus**		
General Reserve	50,000	42,000
Statement of Profit and Loss	1,10,000	78,000
3. **Long Term Borrowings**		
5% Debentures	3,50,000	2,60,000
4. **Trade Payables**		
Creditors	45,000	18,000
Bills Payable	10,000	12,000
5. **Other Current Liabilities**		
Outstanding Expenses	2,000	5,000
6. **Fixed Assets**		
Building	4,40,000	2,90,000
Plant and Machinery	1,60,000	1,90,000
7. **Trade Receivables**		
Debtors	1,55,000	1,30,000
8. **Cash & Bank Balances**		
Cash at Bank	1,39,000	95,000

Additional Information :

(*i*) Depreciation charged on building ₹20,000.

(*ii*) A machine with a book value of ₹10,000 was sold for ₹8,000.

(*iii*) Debentures were issued on 1st April, 2013, at a discount of 10%. The discount was written off from General Reserve. *(ISC Sample Question Paper, 2015)*

SOLUTION : CASH FLOW STATEMENT OF DIAMOND LIMITED

for the year ended 31st March, 2014

Particulars		₹	₹
A. Cash Flows from Operating Activities :			
Profit before Tax$^{(1)}$		49,000	
Adjustments for non-cash and non-operating items :			
Add : Depreciation on Building	20,000		

Depreciation on Plant & Machinery	20,000		
Loss on Sale of Machinery	2,000		
Interest on Debentures (5% on ₹3,50,000)	17,500	59,500	
Operating profit before working capital changes		1,08,500	
Add : Increase in Current Liabilities :			
Creditors		27,000	
		1,35,500	
Less : Decrease in Current Liabilities :			
Bills Payables	2,000		
Outstanding Expenses	3,000		
Increase in Current Assets :			
Debtors	25,000		
Inventories	23,000	53,000	
Net Cash from operating activities		82,500	82,500
B. Cash Flows from Investing Activities :			
Purchase of Building(3)		(1,70,000)	
Sale of Plant(4)		8,000	
Net Cash used in investing activities		(1,62,000)	(1,62,000)
C. Cash Flows from Financing Activities :			
Issue of Equity share capital		60,000	
Issue of Debentures (₹90,000 *less* Discount ₹9,000)		81,000	
Interest paid on Debentures		(17,500)	
Net Cash from financing activities		1,23,500	1,23,500
Net Increase in cash and cash equivalents			44,000
Add : Cash and cash equivalents in the beginning of the period			95,000
Cash and cash equivalents at the end of the period			1,39,000

Working Notes :

(1) Calculation of Profit before Tax :

	₹
Profit & Loss Balance on 31st March, 2014	1,10,000
Less : Profit & Loss Balance on 31st March, 2013	78,000
	32,000
Add : Transfer to General Reserve	17,000
	49,000

(2)

Dr. GENERAL RESERVE ACCOUNT Cr.

Particulars	₹	Particulars	₹
To Discount written off (10% of ₹90,000)	9,000	By Balance b/d	42,000
To Balance c/d	50,000	By Surplus of Statement of Profit & Loss (Balancing figure)	17,000
	59,000		59,000

(3)

BUILDING ACCOUNT

Dr. Cr.

Particulars	₹	Particulars	₹
To Balance b/d	2,90,000	By Depreciation A/c (Current year's depreciation)	20,000
To Bank A/c (Balancing figure, being purchase)	1,70,000	By Balance c/d (Given)	4,40,000
	4,60,000		4,60,000

(4)

PLANT & MACHINERY ACCOUNT

Dr. Dr.

Particulars	₹	Particulars	₹
To Balance b/d	1,90,000	By Bank	8,000
		By Loss on Sale	2,000
		By Depreciation A/c (Current Year's Depreciation)	20,000
		By Balance c/d	1,60,000
	1,90,000		1,90,000

ILLUSTRATION

Arthur Ltd. reported a profit of ₹90,000 for the year ended March 31, 2012, after considering the following :

	₹
(*a*) Tax provided during the year	3,000
(*b*) Amortization of goodwill	12,000
(*c*) Profit on sale of land	5,000
(*d*) Writing off preliminary expenses	2,000
(*e*) Machinery costing ₹40,000 (accumulated depreciation thereon being ₹18,000) was sold during the year at a loss of ₹17,000.	

Extracts of its Balance Sheet at the beginning and at the end of the year are given below :

	01-04-2011	*31-03-2012*
Accounts Receivable	16,000	20,000
Inventory	15,000	12,000
Cash at Bank	10,000	8,000
Accounts Payable	11,000	9,000
Expenses Payable	5,000	6,000
Provision for Taxation	6,000	4,000
Investment (short term)	2,000	5,000
Plant and Machinery (net value)	1,30,000	94,000
Contingent Liability :		
Proposed Dividend	10,000	12,000

You are required to calculate Cash from Operating Activities as per Accounting Standard 3. (Show your working clearly.)

(I.S.C. 2013)

SOLUTION :

Arthur Ltd.

Cash Flow from Operating Activities

for the year ended 31st March, 2012

Particulars		₹
Cash Flow from Operating Activities :		
Net Profit before Tax (Note 1)		1,03,000
Adjustments for Non-Cash and Non-Operating items :		
Add : Goodwill written off		12,000
Preliminary Expenses Written off		2,000
Depreciation (Note 2)		14,000
Loss on Sale of Plant & Machinery		17,000
		1,48,000
Less : Profit on Sale of Land		(5,000)
Operating Profit before Working Capital Changes		1,43,000
Add : Decrease in Current Assets		
Inventory	3,000	
Increase in Current Liabilities		
Expenses Payable	1,000	4,000
		1,47,000
Less : Increase in Current Assets		
Accounts Receivable	(4,000)	
Decrease in Current Liabilities		
Accounts Payable	(2,000)	(6,000)
		1,41,000
Less : Tax Paid (Note 3)		(5,000)
Net Cash Flow from Operating Activities		1,36,000

Notes :

(1) Calculation of Net Profit before Tax :

	₹
Net Profit for the year	90,000
Add : Provision for Tax	3,000
Proposed dividend (for 2011)	10,000
Net Profit before Tax	1,03,000

(2)

Dr. PLANT & MACHINERY ACCOUNT Cr.

Particulars	₹	*Particulars*	₹
To Balance b/d	1,30,000	By Bank	5,000
		By Loss on Sale	17,000
		By Depreciation (Balancing Figure)	14,000
		By Balance c/d	94,000
	1,30,000		1,30,000

(3)

PROVISION FOR TAX ACCOUNT

Dr. Cr.

Particulars	₹	Particulars	₹
To Bank (Balancing Figure)	5,000	By Balance b/d	6,000
To Balance c/d	4,000	By Statement of Profit & Loss	3,000
	9,000		9,000

SHORT ANSWER QUESTIONS — I

(Questions Carrying 2 Marks)

Q. 1. State why Cash Flow Statement is not a substitute for Income Statement?

Ans. Because Cash Flow Statement shows only the inflows and outflows of cash whereas Income Statement shows both cash and non-cash items of revenue nature and also shows the net income during the year.

Q. 2. State whether conversion of debentures into equity shares by a financing company will result in inflow, outflow or no flow of cash.

Ans. No Flow, because Cash is not affected.

Q. 3. What is meant by Cash equivalents? *(I.S.C. 2010)*

Ans. These are short-term highly liquid investments that are readily convertible into known amounts of cash and which present insignificant risk of changes in their values.

Q. 4. List any two items other than cash in hand and cheques in hand that are included in 'Cash and Cash Equivalents'. *(C.B.S.E. 2020, Punjab)*

Ans. Any Two (*i*) Treasury Bills (*ii*) Commercial Paper (*iii*) Current Investments (*iv*) Balance with Banks.

Q. 5. How are various activities classified as per AS-3 (Revised) while preparing Cash Flow Statement?

Ans. As per Accounting Standard-3 (Revised) changes resulting in inflows and outflows of Cash are classified into three types of activities namely :

(*i*) Cash Flows from Operating Activities
(*ii*) Cash Flows from Investing Activities
(*iii*) Cash Flows from Financing Activities

Q. 6. What is meant by Operating Activities?

Ans. Operating activities are the main revenue generating activities of an enterprise.

Q. 7. Give two examples of Cash Flows from Operating Activities.

Ans. (*i*) Cash receipts from the sale of goods and rendering of services.

(*ii*) Cash payments to suppliers for goods and services.

Q. 8. What is meant by Investing Activities?

Ans. Investing activities are the purchase and sale of long-term assets. These assets also include the purchase and sale of such investments which are not included in Cash equivalents.

Q. 9. Give four types Investing Activities. *(I.S.C. 2007)*

Ans. (*i*) Cash payments to acquire fixed assets.

(*ii*) Cash receipts from sale of fixed assets.

(*iii*) Interest Received

(*iv*) Dividend Received

Q. 10. What is meant by Financing Activities?

Ans. Financing activities are the activities that result in change in Capital and borrowings of the enterprise.

Q. 11. Give two examples of Cash Flows from Financing Activities. *(I.S.C. 2008)*

Ans. (*i*) Cash receipts from issuing shares and debentures.

(*ii*) Repayment of debentures.

Q. 12. How do you treat profit or loss on sale of fixed assets for calculating Cash flow from operating activities?

Ans. Loss on sale of fixed assets is added back and profit on sale of fixed assets is deducted from net profit while arriving at the cash flow from operating activities.

Q. 13. Why do we add back depreciation to net profit while calculating cash flows from operating activities?

Ans. Depreciation reduces the net profit without reducing the cash balance as it is a non cash item. Hence, it is added back to net profit in order to find out the operating profit.

Q. 14. Why do we add back preliminary expenses to net profit while calculating cash flows from operating activities?

Ans. When preliminary expenses are written off they are debited to profit & loss account. But the writing off of preliminary expenses does not involve cash payment. Hence, they are added back to net profit for calculating the operating profit.

Q. 15. How will you treat decrease in prepaid expenses in the cash flow from operating activities?

Ans. Decrease in prepaid expenses will be added to operating profit while calculating cash flow from operating activities.

Q. 16. What adjustments are required for decrease or increase in creditors/bills payable while calculating 'Cash flow from operating activities'?

Ans. Decrease in Creditors/bills payable is deducted and Increase in creditors/bills payable is added while calculating Cash flow from operating activities.

Q. 17. For calculating 'Cash flow from operating activities' why decrease in debtors or bills receivables are added to operating profits?

Ans. Decrease in debtors or bills receivables indicate that collection from debtors or bills receivables are more than the amount of credit sale during the year. Hence, the decrease in debtors or bills receivables is added to operating profits for arriving at the figure of net cash generated from operating activities.

Q. 18. How will you deal increase in the balance of 'Securities Premium' while preparing a Cash Flow Statement?

Ans. Increase in balance of securities premium represents the amount of premium received on issue of shares and debentures. It will be shown as 'Cash from Financing Activities'.

Q. 19. Give any one example of an activity, which is an investing activity for every type of enterprise. *(C.B.S.E. 2017, Comptt.)*

Ans. Following are investing activity for every type of enterprise :

- Purchase of Goodwill
- Purchase of Fixed Assets
- Sale of Fixed Assets

Q. 20. Fine Garments Ltd. is engaged in the export of readymade garments. The company purchased a machinery of ₹10,00,000 for the use in packaging of such garments. State giving reason whether the cash flow due to the purchase of machinery will be cash flow from operating activities, investing activities or financing activities?

Ans. Investing Activity. Because Fine Garments Ltd. has purchased the machinery for use in the business not for sale.

Q. 21. *A* Ltd., engaged in the business of retailing of two wheelers, invested ₹50,00,000 in the shares of a manufacturing company. State with reason whether the dividend received on this investment will be Cash Flows from Operating Activities or Investing Activities.

Ans. Dividend received will be cash flow from 'investing activities' because such income is not earned by *A* Ltd. from its principal revenue generating activities.

Q. 22. How will you treat payment of tax and payment of dividend in a Cash flow statement?

Ans. Payment of tax will be deducted under 'Cash flows from operating activities' and payment of dividend will be shown as outflow under 'Cash flows from financing activities'.

Q. 23. How will you treat 'Interest on Debentures' while preparing a Cash Flow Statement?

Ans. It will be added to net profit in operating activities and will also be shown as outflow under financing activities.

Q. 24. State whether cash deposited in bank will result in inflow, outflow or no Flow of cash?

Ans. No flow. Because in a cash flow statement cash includes bank also. Cash deposited in bank merely represents movement between items of cash and cash equivalents.

Q. 25. Give two examples of 'significant non-cash transactions'.

Ans. (*i*) Acquisition of fixed asset by issue of debentures or shares.

(*ii*) Conversion of debentures into shares.

Q. 26. A company receives a dividend of ₹2 Lakhs on its investment in other company's shares. Will it be cash inflow from operating or investing activities?

Ans. It will be Cash inflow from investing activities.

Q. 27. In which category 'Rent received' will be classified while preparing the Cash Flow Statement in case of (*i*) Real Estate Agent and (*ii*) Non-Real Estate Agent.

Ans. (*i*) Rent Received will be Operating Activity in case of Real Estate Agent.

(*ii*) Rent Received will be Investing Activity in case of Non-Real Estate Agent.

Q. 28. State how Cash Flow Statements are historical in nature?

Ans. Cash Flow Statement is historical in nature because it is prepared on the basis of Profit and Loss Statement and Balance Sheet, which is based on past transactions.

Q. 29. Give one difference between an operating activity and an investing activity. *(ISC Sample Paper 2017)*

Ans. Operating activities are related to purchase and sale of goods and services whereas investing activities are related to purchase and sale of long-term assets.

Q. 30. Give one difference between an investing activity and a financing activity.

Ans. Investing activities are related to purchase and sale of long-term assets whereas financing activities are related to activities that result in change in capital and borrowings of the enterprise.

Q. 31. Give two differences between Net Profit and Cash from Operations. *(I.S.C. 2013)*

Q. 32. State, with reason, which of the following would result in inflow, outflow or no flow of cash :

(*i*) Cash deposited in the bank.

(*ii*) Proposed Dividend. *(I.S.C. Specimen Question Paper, 2018)*

Ans.

(*i*)	Cash deposited in the bank.	No effect	Cash and Bank both are parts of Cash and Cash Equivalents.
(*ii*)	Proposed Dividend	No effect	Cash is not affected because proposed dividend will be paid in the next year.

Q. 33. State whether the following would result in inflow, outflow or no flow of cash :

(*i*) Bill Receivable endorsed to Creditors.

(*ii*) Old vehicle written off. *(I.S.E. 2018)*

Ans. (*i*) No Flow; (*ii*) No Flow.

Q. 34. Mention with reason whether the following would result in inflow, outflow or no flow of cash :

(*i*) Issue of fully paid Bonus Shares.

(*ii*) Cash withdrawn from Bank. *(I.S.C. 2019)*

Ans.

(*i*)	Issue of fully paid bonus shares	No Flow	Cash is not affected because it is capitalisation of profits.
(*ii*)	Cash withdrawn from Bank	No Flow	Cash and Bank both are parts of Cash and Cash Equivalents.

Q. 35. Identify the following as operating, investing, financing or Cash & Cash Equivalents :

(*i*) Bank Overdraft repaid.

(*ii*) Purchase of marketable securities to be sold within 90 days. *(I.S.C. 2019)*

Ans. (*i*) Financing Activity; (*ii*) Cash and Cash Equivalent.

SHORT ANSWER QUESTIONS — II

Q. 1. For calculating 'cash flow from operating activities' from the given figure of 'Net Profit' earned during a year, how would you deal with (*a*) Increase in Debtors, (*b*) Decrease in Stock, (*c*) Decrease in Bills Payable, and (*d*) Increase in Creditors?
[**Ans.** (*a*) Less, (*b*) Add, (*c*) Less, and (*d*) Add.]

Q. 2. For calculating 'cash flow from operating activities' from a given figure of 'Net Profit' earned during a year, how would you deal with (*a*) the redemption of debentures, (*b*) decrease in outstanding expenses, (*c*) increase in cash balance, and (*d*) decrease in inventory?
[**Ans.** (*a*) No effect, (*b*) Less, (*c*) No effect, and (*d*) Add.]

Q. 3. Classify the following into Cash flows from (*i*) Operating Activities, (*ii*) Investing Activities, and (*iii*) Financing Activities while preparing a Cash flow statement :

(*a*) Purchase of Fixed Assets;
(*b*) Issue of Share Capital;
(*c*) Payment of Income Tax;
(*d*) Payment of Dividend;
(*e*) Payment of Interest;
(*f*) Sale of Long-term Investments;
(*g*) Interest Received;
(*h*) Dividend Received;
(*i*) Repayment of Long-term Loans.

[**Ans.** Cash from Operating Activities : c,
Cash from Investing Activities : a, f, g, h
Cash from Financing Activities : b, d, e, i]

Q. 4. For each of the following transactions, calculate the resulting cash flow and state the nature of cash flow viz., operating, investing and financing.

(*a*) Acquired machinery for ₹2,50,000 paying 20% down and executing a bond for the balance payable.

(*b*) Paid ₹2,50,000 to acquire shares in Informa Tech. and received a dividend of ₹50,000 after acquisition.

(*c*) Sold machinery of original cost ₹2,00,000 with an accumulated depreciation of ₹1,60,000 for ₹60,000.

[**Ans.** (*a*) Cash used in investing activities ₹50,000.
(*b*) Cash used in investing activities ₹2,00,000.
(*c*) Cash from investing activities ₹60,000.]

Q. 5. How are the various activities classified according to AS-3 (Revised) while preparing the Cash Flow Statement?

[**Ans.** While preparing the cash flow statement according to AS-3 (Revised) various activities are classified into three groups :

1. Net cash flows from operating activities.
2. Net cash flows from Investing activities.
3. Net cash flows from financing activities.]

Q. 6. What is meant by a Cash Flow Statement? *(I.S.C. 2009)*

[**Ans.** A cash flow statement is a statement showing changes i.e. inflows and outflows of cash and cash equivalents during a particular period. Cash equivalents are short-term, highly liquid investments that are readily convertible into cash. Cash flow statement shows :

(*i*) Net cash flows from operating activities.
(*ii*) Net cash flows from Investing activities.
(*iii*) Net cash flows from financing activities.
(*iv*) Net changes in cash and cash equivalents.]

Q. 7. Classify the following into cash flow from (*i*) Operating Activities; (*ii*) Investing Activities and (*iii*) Financing Activities while preparing a Cash Flow Statement :

(*i*) Purchase of Machinery
(*ii*) Issue of Debentures
(*iii*) Payment of Dividend
(*iv*) Payment of Income Tax

Ans. (*i*) Investing Activities.
(*ii*) Financing Activities.
(*iii*) Financing Activities.
(*iv*) Operating Activities.]

Q. 8. What is a Cash Flow Statement? List any two objectives of preparing the statement.

[**Ans.** A Cash flow statement is a statement that shows inflows and outflows of Cash and Cash equivalents during a particular span of time. It shows the net increase and decrease of Cash and Cash equivalents under operating, investing and financing activities separately and collectively.

Objectives : (*i*) To ascertain the sources (*i.e.*, Operating/Investing/Financing Activities) from which Cash and Cash equivalents were generated by an enterprise.

(*ii*) To ascertain the uses (*i.e.*, Operating/Investing/Financing Activities) for which Cash and Cash equivalents were used by an enterprise.

Q. 9. Classify the following into cash flows from Investing activities/Financing activities while preparing a Cash Flow Statement :

(*a*) Repayment of Public Deposits
(*b*) Sale of Fixed Assets
(*c*) Receipt of Dividend
(*d*) Interest Received.

[**Ans.** (*a*) Financing Activities
(*b*) Investing Activities
(*c*) Investing Activities
(*d*) Investing Activities]

Q. 10. Classify the following into cash flows from Investing activities/Financing activities while preparing a Cash Flow Statement :

(*a*) Repayment of Bank Loan
(*b*) Purchase of Fixed Assets

(*c*) Payment of Dividend
(*d*) Interest Received

[**Ans.** (*a*) Financing Activities
(*b*) Investing Activities
(*c*) Financing Activities
(*d*) Investing Activities]

Q. 11. Categorise each of the following items into operating/investing/financing activities while preparing the Cash Flow Statement :

(*a*) Redemption of 2,00,000, 12% preference shares of ₹10 each at a premium of ₹4 per share.
(*b*) Sale of Machinery for ₹40,000.
(*c*) Declared and paid dividend ₹1,00,000.
(*d*) Interest collected from Investments ₹28,000.

Ans. (*a*) Financing Activity
(*b*) Investing Activity
(*c*) Financing Activity
(*d*) Investing Activity.

Q. 12. State what would constitute the operating activities for the following types of enterprises :

(*i*) Real Estate Business
(*ii*) Cotton Textile Mill
(*iii*) Financial Enterprise
(*iv*) Hotel
(*v*) Film Production Unit.

Ans. (*i*) **Real Estate Business** : Its operating activities are purchase and sale of land and building and receiving of rent.

(*ii*) **Cotton Textile Mill** : Its operating activities are purchase of cotton, manufacture and sale of yarn and cloth.

(*iii*) **Financial Enterprise** : Its operating activities are borrowing and lending of funds, receipt of interest and dividend, payment of interest etc.

(*iv*) **Hotel** : Its operating activities are renting of rooms, providing food and beverages to customers, purchase of grocery items etc.

(*v*) **Film Production Unit** : Its operating activities are making of films and selling the same to distributors.

PRACTICAL QUESTIONS

(Q. Nos. 1 to 53 are strictly in the serial order of Illustrations)

Q. 1. Identify the following transactions as belonging to (*i*) Operating, (*ii*) Investing, (*iii*) Financing Activities and (*iv*) Cash Equivalents :

1. Interest paid
2. Interest received by a Company on its investments *(ISC 2016)*
3. Dividend received
4. Dividend paid

5. Cash received from sale of goods
6. Cash paid for purchase of Stock in Trade
7. Salaries and Wages paid
8. Debentures purchased
9. Loan advanced
10. Sale of fixed assets
11. Bank balance
12. Short-term deposits in banks
13. Bank Overdraft
14. Marketable Securities
15. Goodwill Written off

(ISC 2016)

[**Ans.** (*i*) Operating Activities : 5, 6, 7, 15
(*ii*) Investing Activities : 2, 3, 8, 9, 10
(*iii*) Financing Activities : 1, 4, 13
(*iv*) Cash Equivalents : 11, 12, 14]

Q. 2. Classify the following activities into (*i*) Operating Activities, (*ii*) Investing Activities, and (*iii*) Financing Activities :

1. Purchase of Shares of a Company.
2. Proceeds from sale of Shares.
3. Brokerage paid on purchase of Shares.
4. Loans and Advances made to third parties.
5. Dividend and interest received on Securities.
6. Salary paid to employees.
7. Interest paid on debentures.
8. Dividend paid to Shareholders.

[**Ans.**

Transaction 1 to 5 : Investing Activities
Transaction 6 : Operating Activities
Transaction 7 & 8 : Financing Activities]

Q. 3. Classify the following transactions as (*i*) Operating Activities; (*ii*) Investing Activities; (*iii*) Financing Activities and (*iv*) Cash and Cash Equivalents.

1. Purchase of Shares
2. Buy-back of Equity Shares
3. Payment of Share issue expenses
4. Discount allowed to Customers
5. Discount received from Suppliers.
6. Increase in the Balance of Cash Credit
7. Repayment of Long-term Loan
8. Repayment of Short-term Loan
9. Proceeds from Short-term Borrowings
10. Dividend paid on Preference Shares
11. Short-term deposits in Bank
12. Rent received by a Company whose main business is Real Estate Business.
13. Rent received by a Company whose main business is manufacturing.

Ans. Operating Activities : 4, 5, 12
Investing Activities : 1, 13

Financing Activities : 2, 3, 6, 7, 8, 9, 10
Cash and Cash Equivalents : 11

Q. 4. State which of the following would result in inflow/outflow of Cash or Cash Equivalents :

(*i*) Purchase of Goods on Credit.
(*ii*) Sale of Goods costing ₹20,000 for ₹15,000 for cash.
(*iii*) Purchase of a fixed asset on long term deferred payment basis.
(*iv*) Issue of shares against purchase of fixed asset.
(*v*) Cash received from a Trade Receivable ₹10,000, discount allowed ₹1,000.
(*vi*) Sale of fixed asset (book value ₹25,000) for ₹20,000 for cash.
(*vii*) Old Furniture (book value ₹10,000) written off. *(I.S.C. 2018)*
(*viii*) Bill Receivable endorsed to creditors. *(I.S.C. 2018)*
(*ix*) Discount of ₹2,000 received while making payment to a creditor of ₹20,000.
(*x*) Cash deposited into Bank.
(*xi*) Sale of Marketable Securities for cash.
(*xii*) Sale of Long-term Investments for cash.
(*xiii*) Conversion of Debentures into Shares.
(*xiv*) Declaration of Dividend. *(ISC Sample paper, 2017)*
(*xv*) Payment of Dividend.
(*xvi*) Receipt of Interest on Investment.
(*xvii*) Receipt of Dividend.

[**Ans.** Inflow : (*ii*) Inflow ₹15,000; (*v*) Inflow ₹10,000; (*vi*) Inflow ₹20,000; (*xii*); (*xvi*); (*xvii*).

Outflow : (*ix*) Outflow ₹18,000; (*xiv*); (*xv*).

No Effect : (*i*); (*iii*); (*iv*); (*vii*); (*viii*); (*x*); (*xi*); (*xiii*)]

Q. 5. State which of the following would result in inflow, outflow or no flow of cash :

1. A long-term loan from a bank.
2. Repayment of long-term loan.
3. Payment of interest on loan.
4. Conversion of debentures into preference shares.
5. Interest received on investments.
6. Interest due on debentures.
7. Receipt of accrued interest.
8. Purchase of securities of a company.
9. Buy-back of Equity Shares.
10. Purchase of Goodwill.
11. Goodwill written off.
12. Patents written off.

[**Ans.** Inflow : 1, 5, 7; Outflow : 2, 3, 8, 9, 10; No effect : 4, 6, 11, 12.]

Cash Flow from Operating Activities

Q. 6 (A). Calculate 'Cash from operating activities' from the following balances :

	31.3.2021 ₹	31.3.2022 ₹
Debtors	50,000	40,000
Bills Receivable	10,000	12,500
Creditors	25,000	20,000
Outstanding Expenses	800	1,000
Bills Payable	40,000	25,000
Accrued Income	6,000	7,000

Operating profit before working capital changes was ₹1,30,000.

[**Ans.** Cash from operating activities ₹1,16,700.]

Q. 6 (B). Calculate 'Cash from operating activities' from the following figures :

	31.3.2021 ₹	31.3.2022 ₹
Operating profit before working capital changes	—	1,50,000
Trade Receivables	3,00,000	3,36,000
Inventory	2,00,000	1,80,000
Prepaid Expenses	20,000	25,000
Accrued Income	8,000	6,000
Trade Payables	1,00,000	1,40,000
Outstanding Expenses	32,000	26,000
Income Received in Advance	3,000	2,000

[**Ans.** Cash from Operating activities ₹1,64,000.]

Q. 7. Calculate 'Cash from operating activities' from the following :—

(*i*) Profits made during the year ₹2,50,000 after considering the following items :—

	₹
(*a*) Depreciation on fixed assets	10,000
(*b*) Amortization of Goodwill	5,000
(*c*) Loss on sale of Machinery	7,000
(*d*) Profit on sale of Land	3,000

(*ii*) **Additional Information :**

	31.3.2022 ₹	31.3.2021 ₹
Trade Receivables	23,000	22,000
Trade Payables	10,000	15,000
Prepaid Expenses	4,000	6,000

[**Ans.** Cash from Operating activities ₹2,65,000.]

Q. 8. On March 31st, 2022 Ramesh and Co. indicated a profit of ₹1,25,000, after considering the following :

	₹
Depreciation on buildings	25,000
Depreciation on plant and machinery	45,000
Amortization of goodwill	20,000
Gain on sale of machinery	10,000

Additional Information :

	31.3.2022 ₹	31.3.2021 ₹
Trade Receivables	45,000	35,000
Inventory on Hand	69,000	75,000
Cash in Hand	30,000	18,000
Trade Payables	32,000	30,000
Expenses payable	5,000	10,000
Bank overdraft	35,000	60,000

Ascertain the net cash (cash flow) from operating activities.

[**Ans.** Cash from Operating activities ₹1,98,000.]

Hints : (1) There will be no entry of Cash in Hand.

(2) Decrease in Bank Overdraft will be recorded under 'Financing Activities'.

Q. 9. Narula Ltd. earned a profit of ₹2,00,000 after charging or crediting the following items :—

	₹
(*i*) Depreciation on Fixed Assets	25,000
(*ii*) Loss on Sale of Furniture	3,000
(*iii*) Amortization of Development Cost	8,000
(*iv*) Provision for Doubtful Debts	2,400
(*v*) Provision for Taxation	40,000
(*vi*) Transfer to General Reserve	20,000
(*vii*) Gain on Sale of Machinery	9,000

The following additional information is given to you :—

	31st March, 2022 ₹	31st March, 2021 ₹
Trade Receivables	1,00,000	90,000
Trade Payables	60,000	41,000
Outstanding Expenses	1,000	5,000
Prepaid Expenses	2,000	—

You are required to determine the Cash from operating activities.

[**Ans.** Cash from operating activities ₹2,52,400.]

Hint. It will be assumed that provision for taxation made during the year equals the payment of taxation during the year.

Q. 10. Z Ltd. made a profit of ₹20,00,000 after charging Depreciation of ₹1,50,000, writing off preliminary expenses of ₹10,000 and loss on sale of assets ₹30,000. The other information available to you is as follows :

At the end of the year Trade Payables showed an increase of ₹45,000; Trade Receivables an increase of ₹53,000; Prepaid Expenses decrease of ₹2,000; and Outstanding Expenses decrease of ₹10,000.

You are required to ascertain cash flow from operating activities.

[**Ans.** Net cash from operating activities ₹21,74,000.]

Q. 11 (A). Calculate 'Cash from Operating activities' from the following figures :—

	31.3.2017	31.3.2018
	₹	₹
Profit and Loss Balance	60,000	65,000
Trade Receivables	1,49,000	1,53,000
General Reserve	2,02,000	2,37,000
Salary Outstanding	30,000	12,000
Wages Prepaid	5,000	7,000
Goodwill	80,000	70,000
Cash and Bank Balance	40,000	30,000

[**Ans.** Cash from Operating activities ₹26,000.]

Hint. Cash and Bank Balance will not affect Cash Flow from Operating Activities.

Q. 11 (B). Calculate 'Cash from operating activities' from the following :—

	31.3.2017	31.3.2018
	₹	₹
Profit and Loss Balance	20,000	30,000
Trade Receivable	14,000	18,000
Provision for Depreciation	30,000	32,000
Outstanding Rent Payable	1,600	4,000
Prepaid Insurance	1,400	1,200
Goodwill	20,000	16,000
Inventories	14,000	18,000

[**Ans.** Cash from operating activities ₹10,600.]

Q. 11 (C). From the following figures calculate 'cash from operating activities' :

	31.3.2017	31.3.2018
	₹	₹
Profit & Loss Balance	5,00,000	3,00,000
Accumulated Depreciation	80,000	1,20,000
Debenture Sinking Fund	1,00,000	1,25,000
Development Rebate Reserve	60,000	70,000
Outstanding Expenses	16,000	24,000
Trade Payables	75,000	91,000
Prepaid Salaries	5,000	2,000

Goodwill	20,000	15,000
Trade Receivables	2,10,000	2,40,000

[**Ans.** Cash used (or lost) in operating activities ₹1,23,000.]

Q. 11 (D). Calculate 'cash from operating activities' from the following :—

(I) Profit for the year amounted to ₹50,000 after providing for depreciation of ₹20,000.

(II) Following is the position of current assets and current liabilities :—

	31.3.2017 ₹	*31.3.2018* ₹
Cash in Hand	15,000	28,000
Trade Receivables	1,00,000	70,000
Provision for Doubtful Debts	5,000	6,000
Trade Payables	80,000	75,000
Inventories	1,20,000	1,60,000
Outstanding Expenses	—	10,000
Prepaid Expenses	8,000	2,000
Accrued Income	10,000	15,000
Income Received in Advance	6,000	3,000
Bank Overdraft	75,000	60,000

[**Ans.** Cash from operating activities ₹64,000.]

Hint. Decrease in Bank Overdraft will be recorded under 'Financing Activities'.

Q. 12. Calculate 'Cash from operating activities' from the following :—

	31.3.2017 ₹	*31.3.2018* ₹
Profit & Loss Balance	60,000	50,000
Inventory	2,00,000	2,40,000
Trade Receivables	80,000	75,000
Outstanding Expenses	7,000	—
Prepaid Expenses	6,000	10,000
Trade Payables	45,000	58,000
Cash in Hand	32,000	44,000

[**Ans.** Cash used (or lost) in operating activities ₹43,000.]

Q. 13. Following is the position of Current Assets and Current Liabilities of *X* Ltd.:—

	31.3.2018 ₹	*31.3.2017* ₹
Creditors	85,000	70,000
Debtors	1,40,000	2,00,000
Bills Receivable	15,000	10,000
Short-term loans	20,000	—
Provision for bad-debts	7,000	10,000

Bank Overdraft	50,000	40,000
Goodwill	1,20,000	1,50,000

The company incurred a loss of ₹37,000 during the year. Calculate 'Cash from operating activities'.

[Ans. Cash from operating activities ₹30,000.]

Hints :

(i) Short term Loan and Bank Overdraft will be treated as financing activity.

(ii) Increase in Goodwill is treated as purchase of Goodwill. Hence, it will not affect 'Cash from operating activities'. It will be shown as an Investing Activity while preparing Cash Flow Statement.

Q. 14. Calculate cash from operating activities from the following Balance Sheets of Himalya Ltd.

Particulars	*Note No.*	*31.3.2018*	*31.3.2017*
I. EQUITY AND LIABILITIES :		₹	₹
(1) **Shareholder's Funds :**			
(a) Share Capital		4,00,000	3,00,000
(b) Reserve and Surplus	1	1,70,000	80,000
(2) **Non-Current Liabilities**			
Long-term Borrowings	2	1,50,000	1,00,000
(3) **Current Liabilities :**			
Trade Payables		40,000	60,000
TOTAL		7,60,000	5,40,000
II. ASSETS :			
(1) **Non-Current Assets :**			
(a) Fixed Assets	3	5,50,000	3,30,000
(b) Non-Current Investments	4	50,000	40,000
(2) **Current Assets :**			
(a) Trade Receivables		83,000	1,14,000
(b) Cash and Bank Balances		77,000	56,000
TOTAL		7,60,000	5,40,000

Notes : (1) Reserve & Surplus :	*31.3.2018*	*31.3.2017*
	₹	₹
General Reserve	1,20,000	1,00,000
Profit & Loss Balance	50,000	(20,000)
	1,70,000	80,000
(2) Long-term Borrowings :		
9% Debentures	1,50,000	1,00,000
(3) Fixed Assets :		
Machinery	7,00,000	4,40,000
Less : Provision for Depreciation	1,50,000	1,10,000
	5,50,000	3,30,000

(4) Rate of Interest on Investments is 8% p.a.

Additional Information :

(*i*) Additional Debentures were issued on 1st April 2017.
(*ii*) Additional investments were made on 1st April 2017.

[**Ans.** Net cash from Operating Activities ₹1,50,500.]

		₹
Hints : (*i*)	Profit during the year :	
	(–) Negative Balance of P & L on 31.3.2017	(20,000)
	(+) Positive Balance of P & L on 31.3.2018	50,000
		70,000

(*ii*) Bracket denotes negative balance.

Q. 15. Calculate 'Cash from Operating Activities' from the following Balance Sheets :

Particulars	*Note No.*	*31.3.2019*	*31.3.2018*
I. EQUITY AND LIABILITIES :		₹	₹
(1) Shareholder's Funds :			
(*a*) Share Capital		5,00,000	5,00,000
(*b*) Reserve and Surplus		2,00,000	1,20,000
(2) Non-Current Liabilities			
Long-term Borrowings	1	2,50,000	2,00,000
(3) Current Liabilities			
(*a*) Other Current Liabilities	2	—	3,000
(*b*) Short Term Provision	3	75,000	70,000
TOTAL		10,25,000	8,93,000
II. ASSETS :			
(1) Non-Current Assets		5,00,000	4,00,000
(2) Current Assets :			
(*a*) Inventory		2,40,000	2,00,000
(*b*) Trade Receivables		2,00,000	1,80,000
(*c*) Cash and Bank Balances		70,000	90,000
(*d*) Other Current Assets	4	15,000	23,000
TOTAL		10,25,000	8,93,000

Notes :	*31.3.2019*	*31.3.2018*
(1) Long-term Borrowings	₹	₹
8% Debentures	2,50,000	2,00,000
(2) Other Current Liabilities : Outstanding Expenses	—	3,000
(3) Short term Provision : Provision for Tax	75,000	70,000
(4) Other Current Assets : Prepaid Expenses	15,000	23,000

[**Ans.** Cash from Operating activities ₹46,000]

Note : It has been assumed that new debentures have been issued on 31.3.2019. As such, interest on debentures has been calculated on ₹2,00,000.

Q. 16. The following is the Statement of Profit and Loss of Z Ltd. for the year ended March 31, 2018 :

Particulars	*Amount*
	₹
I. Revenue from Operations	40,00,000
II. Expenses :	
Purchases	22,00,000
Changes in Inventories (Opening Inventory – Closing Inventory) (₹8,00,000 – ₹9,00,000)	(1,00,000)
Depreciation and Amortization Expenses	80,000
Other Expenses	10,20,000
Total Expenses	32,00,000
III. Profit before Tax (I – II)	8,00,000

Additional Information :

(*i*) Sundry Creditors increased by ₹40,000 during the year.
(*ii*) Sundry Debtors increased by ₹70,000 during the year.
(*iii*) Outstanding wages decreased by ₹10,000 during the year.
(*iv*) Bills Receivable decreased by ₹5,000 during the year.
(*v*) Prepaid expenses decreased by ₹20,000 during the year.

Compute net Cash from operations by the indirect method.

[**Ans.** Net Cash from operating activities ₹7,65,000]

Q. 17 (A). From the following information, calculate 'cash inflows from operating activities' :—

	₹
Profit & Loss Balance 1-4-2021 (Credit)	5,50,000
Profit & Loss Balance 31-3-2022 (Credit)	8,00,000
Amount transferred to General Reserve	50,000
Income Tax Provision made	1,50,000
Discount on Issue of Debentures written off	10,000
Prepaid Expenses on 1-4-2021	8,000
Loss on Sale of Furniture	1,000
Income from Investment	4,000

[**Ans.** Cash from operating activities ₹3,15,000.]

Note : It is assumed that Income tax paid during the year is equivalent to provision for Income-Tax made during the year. As such, in addition to adding back in profits, it will also be deducted at the end as tax paid.

Q. 17 (B). From the following information, calculate 'Cash from operating activities':

	₹
Profit & Loss Balance on 1-4-2017 (Debit)	12,000
Profit & Loss Balance on 31-3-2018 (Credit)	60,000

Writing off Preliminary Expenses	10,000
Transfer to General Reserve	40,000
Transfer to Provision for Doubtful Debts	6,000
Increase in Trade Receivables	32,000
Trade Payables on 1-4-2017	60,000
Trade Payables on 31-3-2018	52,000
Prepaid Expenses on 1-4-2017	7,500
Prepaid Expenses on 31-3-2018	5,000
Outstanding Expenses on 1-4-2017	4,000

[**Ans.** Cash from operating activities ₹86,500.]

Hint :— Net Profit as per Profit & Loss A/c = ₹12,000 + ₹60,000 = ₹72,000.

Cash Flow from Investing Activities :

Q. 18. From the following particulars, calculate cash flows from investing activities :

	Purchased ₹	*Sold* ₹
Land & Building	5,00,000	—
Machinery	3,40,000	4,50,000
Investments	4,10,000	1,50,000
Patents	—	60,000

Dividend received on shares held as Investments	₹10,000
Interest received on debentures held as Investments	₹ 8,000
Dividend paid on equity share capital	₹50,000

[**Ans.** Net Cash used in Investing Activities ₹5,72,000.]

Q. 19. *X* Ltd. has Plant and Machinery whose written down value on 1st April, 2021 was ₹15,40,000 and on 31st March, 2022 was ₹19,10,000. Depreciation for the year was ₹1,50,000. In the beginning of the year, a part of plant was sold for ₹2,20,000 which had a written down value of ₹3,00,000.

Calculate Cash Flow from Investing Activities.

[**Ans.** Net Cash used in Investing Activities ₹6,00,000.]

Hint. Cash used for purchase ₹8,20,000 and Cash inflow from sale ₹2,20,000

Q. 20. Calculate Cash Flow from Investing Activities from the following particulars :

	1st April, 2017 ₹	*31st March, 2018* ₹
Plant & Machinery (Written Down Value)	12,00,000	15,40,000

Information :

(*i*) Depreciation charged during the year ₹2,20,000

(*ii*) Plant & Machinery costing ₹2,40,000 on which ₹90,000 had accumulated as depreciation was sold for ₹1,70,000.

[**Ans.** Net cash used in Investing Activities ₹5,40,000.]

Hint : Cash used for purchase ₹7,10,000 and cash inflow from sale ₹1,70,000.

Q. 21. Calculate Cash Flows from Investing Activities from the following information :

Particulars	*31st March 2022*	*31st March 2021*
	₹	₹
Investments in Land	16,00,000	6,00,000
10% Long Term Investments	2,50,000	4,00,000
Plant and Machinery	3,00,000	2,00,000
Goodwill	80,000	15,000

Additional information :

A machine costing ₹40,000 (depreciation provided thereon ₹12,000) was sold for ₹35,000. Depreciation charged during the year was ₹60,000.

[**Ans.** Net Cash used in Investing Activities ₹10,28,000.]

Notes :

(*i*) It is assumed that investments were sold on 31st March, 2022.

(*ii*) In case it is assumed that investments were sold on 1st April, 2021, interest would be ₹25,000 and Cash used in investing activities would be ₹10,43,000.

Q. 22. From the following information, calculate the Cash Flow from Investing Activities of *X* Ltd.:

Particulars	*31st March, 2021*	*31st March, 2022*
	₹	₹
1. Non-Current Investments	8,00,000	10,00,000
2. Fixed Assets	15,00,000	18,20,000

Additional Information :

(*i*) Half of the Non-Current investments held in the beginning of the year were sold at 15% profit.

(*ii*) Depreciation on Fixed Assets was ₹1,60,000 for the year.

(*iii*) Interest received on Non-Current investments : ₹50,000.

(*iv*) Dividend received on Non-Current investments : ₹20,000.

(*v*) Rent received : ₹25,000.

[**Ans.** Net Cash used in Investing Activities ₹5,25,000.]

Q. 23. The balance in Plant & Machinery account and Accumulated depreciation account as on March 31, 2021 and 2022 stood as follows :

	31st March, 2021	*31st March, 2022*
	₹	₹
Plant & Machinery	48,00,000	65,40,000
Accumulated Depreciation	14,05,000	22,10,000

Plant & machinery costing ₹12,80,000 accumulated depreciation thereon ₹5,30,000 was sold at a loss of ₹2,60,000.

You are required to :

(*i*) Compute the amount of plant and machinery purchased, sold and depreciation charged for the year.

(*ii*) How each of the item related to plant & machinery will be reported in the statement of cash flows.

[**Ans.** (*i*) Inflow from sale of plant & machinery ₹4,90,000 and outflow on purchase of plant & machinery ₹30,20,000 will be reported under the head 'Cash flow from investing activities.'

(*ii*) Loss on sale of plant & machinery ₹2,60,000 and current year's depreciation ₹13,35,000 will be added to net profit while computing cash flow from operating activities.]

Q. 24. From the following particulars, calculate Cash from Investing Activities :

Particulars	*Opening Balances*	*Closing Balances*
	₹	₹
Plant & Machinery (at cost)	8,00,000	7,60,000
Accumulated Depreciation	2,70,000	3,15,000
Patents	3,20,000	2,10,000
Goodwill	1,50,000	1,20,000

Additional Information :

During the year :

(*i*) Depreciation charged on Plant and Machinery ₹80,000.

(*ii*) A machine having a book value of ₹1,40,000 was sold for ₹1,50,000.

(*iii*) Patents having a book value of ₹60,000 were sold for 45,000.

[**Ans.** Net Cash Flow from Investing Activities ₹60,000.]

Q. 25. The balance in Plant & Machinery account and Accumulated depreciation account as on March 31, 2021 and 2022 stood as follows :

	31st March, 2021	*31st March, 2022*
	₹	₹
Plant & Machinery	45,20,000	62,50,000
Accumulated Depreciation	12,60,000	14,10,000

Plant & Machinery costing ₹8,00,000 was sold at a loss of ₹1,04,000. Depreciation provided during the year was ₹4,30,000.

You are required to calculate Cash from Investing Activities.

[**Ans.** Inflow from sale of plant & machinery ₹4,16,000 and outflow on purchase of plant & machinery ₹25,30,000 will be reported under the head 'Cash flow from investing activities.']

Q. 26 (A). D.K. Ltd. provides you the following information :—

Non-Current Investments as on 31-3-2021	₹1,20,000
Non-Current Investments as on 31-3-2022	₹ 40,000

During the year 2022, the company sold 80% of its original investments at a profit of 20% on book value. Calculate sources and uses of cash.

[**Ans.** Sources ₹1,15,200; Uses ₹16,000.]

Hint :— Prepare Non-Current Investments A/c.

Q. 26 (B). *X* Ltd. provides you the following information :

Non-Current Investments as on 31-3-2021	₹50,000
Non-Current Investments as on 31-3-2022	₹60,000

During the year 2022, *X* Ltd. purchased investments costing ₹25,000 and sold some investments at a loss of 20% on book value. Calculate sources of cash.

[**Ans.** Sources ₹12,000.]

Q. 27. From the following information, calculate cash flows from investing activities :

	31.3.2021	31.3.2022
	₹	₹
Plant and Machinery	12,00,000	15,00,000
Investments (Long-term)	1,50,000	4,20,000
Land (at Cost)	5,00,000	4,00,000

Additional Information :

(*i*) Depreciation charged on Plant and Machinery ₹72,000.

(*ii*) Plant and Machinery with a book value of ₹1,20,000 was sold for ₹75,000.

(*iii*) Investments were purchased for ₹3,00,000. Some investments were sold at a loss of ₹10,000. Interest received on investments during the year ₹15,000.

(*iv*) Land was sold at a profit of ₹80,000.

[**Ans.** Net Cash used in Investing Activities ₹5,02,000.]

Cash Flow from Financing Activities

Q. 28. Calculate Cash flows from financing activities from the following particulars :

	March 31, 2018	*March 31, 2017*
	₹	₹
Equity Share Capital	12,00,000	7,00,000
8% Preference Share Capital	—	1,00,000
9% Debentures	2,00,000	—
7% Debentures	—	1,00,000

Additional Information :

(*i*) Equity Shares were issued at a premium of 2%.

(*ii*) 8% Preference Shares were redeemed at a premium of 2%.

(*iii*) 9% Debentures were issued at a discount of 1% and 7% debentures were redeemed at a premium of 5%.

(*iv*) Underwriting commission on Equity Shares was paid @ 2.5% on issue price.

(*v*) Interest paid on 7% debentures ₹7,000.

(*vi*) Dividend paid on preference shares ₹8,000.

[**Ans.** Net Cash from financing activities ₹4,73,250.]

Note : Underwriting Commission will be ₹12,750 *i.e.*, 2.5% on (₹5,00,000 + Premium ₹10,000).

Q. 29. From the following Balance Sheets of Enclotek Ltd. as at 31st March and the additional information provided, calculate (*i*) Cash from 'Operating Activities' and (*ii*) Cash from 'Financing Activities' :

Particulars	*Note No.*	*31.3.2018*	*31.3.2017*
		₹	₹
I. EQUITY AND LIABILITIES :			
(1) Shareholder's Funds :			
(*a*) Share Capital	1	7,00,000	7,50,000
(*b*) Reserve and Surplus	2	3,35,000	—
(2) Non-Current Liabilities			
Long-term Borrowings	3	3,00,000	2,00,000
(3) Current Liabilities		70,000	1,10,000
TOTAL		14,05,000	10,60,000
II. ASSETS :			
(1) Non-Current Assets :			
(*a*) Fixed Assets			
(*i*) Tangible Assets		8,60,000	6,20,000
(*ii*) Intangible Assets	4	—	20,000
(*b*) Non-Current Investments		1,25,000	80,000
(2) Current Assets		4,20,000	3,40,000
TOTAL		14,05,000	10,60,000

Notes :

	31-3-2018	*31-3-2017*
(1) Share Capital :	₹	₹
Equity Share Capital	5,00,000	4,50,000
5% Preference Share Capital	2,00,000	3,00,000
	7,00,000	7,50,000
(2) Reserve & Surplus :		
Capital Redemption Reserve	1,00,000	—
General Reserve	1,35,000	1,00,000
Profit & Loss Balance	1,00,000	(1,00,000)
	3,35,000	—
(3) Long-term Borrowings :		
8% Debentures	3,00,000	2,00,000
(4) Intangible Assets :		
Goodwill	—	20,000

Additional Information :

(*i*) Depreciation provided on Fixed Assets ₹60,000.

(*ii*) Preference shares were redeemed at a premium of 5% on 31st March, 2018.

(*iii*) Additional debentures were issued on 1st October, 2017.

(*iv*) Proposed dividend on equity share capital for previous year ended 31st March 2017 was paid @ 8%.

[**Ans.** (*i*) Net Cash flows from Operating Activities ₹3,71,000;
(*ii*) Net Cash used in Financing Activities ₹26,000.]

Hint : Dividend paid on Preference Shares ₹15,000.

Notes : (1) Negative balance of Profit & Loss amounting to ₹1,00,000 appearing in the Balance Sheet on 31.3.2017 represents an amount of loss. In the current year (2017-18), after covering this loss of ₹1,00,000, the Profit and Loss shows a profit of ₹1,00,000. It means net profit during the current year must have been ₹1,00,000 + ₹1,00,000 = ₹2,00,000.

(2) Interest on Debentures :

8% on ₹2,00,000 for 6 months	8,000
8% on ₹3,00,000 for 6 months	12,000
	20,000

(3) Since dividend on Equity Shares has been paid, dividend on Preference Shares also must have been paid prior to dividend on equity shares.

(4) Proposed Dividend paid on Equity Share Capital ₹36,000.

Q. 30. Sony Ltd. provides you the following information. Calculate Cash flows from financing activities :

Particulars	*31st March, 2018*	*31st March, 2017*
	₹	₹
Equity Share Capital	12,50,000	10,00,000
8% Preference Share Capital	2,00,000	—
10% Debentures	—	3,00,000
Investment in Shares	1,50,000	1,00,000

Additional Information :

(*i*) During the year 2017-18, Sony Ltd. issued bonus shares in the ratio of 4 : 1 by capitalising reserve.

(*ii*) 10% Debentures were redeemed on 1 Jan., 2018 at a premium of 5%.

(*iii*) Preference Dividend paid ₹8,000.

(*iv*) Dividend received on Investments ₹10,000.

[**Ans.** Cash used in Financing Activities ₹1,45,500.]

Q. 31. From the following information, Calculate :

(*i*) Cash Flows from Investing Activities, and

(*ii*) Cash Flows from Financing Activities.

	31st March, 2018	31st March, 2017
Plant & Machinery	10,30,000	8,50,000
Accumulated Depreciation on Plant & Machinery	2,68,000	2,20,000
8% Debentures	3,50,000	5,00,000
Bank Overdraft	3,00,000	2,10,000

Additional Information :

(*i*) During the year a machine costing ₹1,50,000 was sold at a loss of ₹44,000. Depreciation on Plant & Machinery charged during the year amounted to ₹80,000.

(*ii*) Interest paid on Bank Overdraft amounted to ₹28,000.

(*iii*) Debentures were redeemed on 1st October 2017 at a premium of 4%.

[**Ans.** (*i*) Net Cash used in Investing Activities ₹2,56,000.
(*ii*) Net Cash used in Financing Activities ₹1,28,000.]

Preparation of Cash Flow Statement

Q. 32. Following are the Balance Sheets of Quick Gains Ltd. :—

Particulars	*Note No.*	*31.3.2018*	*31.3.2017*
I. EQUITY AND LIABILITIES :		₹	₹
(1) Shareholder's Funds :			
(*a*) Share Capital		2,00,000	2,00,000
(*b*) Reserve and Surplus		1,25,000	20,000
(2) Non-Current Liabilities :			
Long-term Borrowings		75,000	50,000
(3) Current Liabilities :			
(*a*) Trade Payables		64,000	90,000
(*b*) Short term Provisions (Provision for Tax)		15,000	10,000
TOTAL		4,79,000	3,70,000
II. ASSETS :			
(1) Non-Current Assets :			
Fixed Assets	1	3,23,000	1,84,000
(2) Current Assets :			
(*a*) Inventory		72,000	50,000
(*b*) Trade Receivables		51,000	75,000
(*c*) Cash & Bank Balances		33,000	59,000
(*d*) Other Current Assets	2	—	2,000
TOTAL		4,79,000	3,70,000

Notes :

	31.3.2018	31.3.2017
	(₹)	(₹)
(1) Fixed Assets :	3,75,000	2,20,000
Less : Accumulated Depreciation	52,000	36,000
	3,23,000	1,84,000

(2) Other Current Assets : Prepaid Expenses	—	2,000

Additional Information :

(1) Contingent Liability

	31st March, 2018 (₹)	31st March, 2017 (₹)
Proposed Dividend	28,000	20,000

(2) Interest paid on long-term borrowings amounted to ₹8,000.

You are required to prepare a Cash-Flow Statement.

[**Ans.** Cash from operating activities ₹1,32,000; Cash used in investing activities ₹1,55,000; and Cash used in financing activities ₹3,000.]

Hint : Proposed Dividend for previous year *i.e.*, for the year ended 31st March 2017 will be added to Net Profit before Tax and will also be shown as Outflow under financing activities. There will be no effect of proposed dividend for the year ended 31st March, 2018.

Q. 33. From the following Balance Sheet of Ajanta Limited as at March 31, 2017, prepare a Cash Flow Statement:

Particulars	*Note No.*	*31-3-2017 (₹)*	*31-3-2016 (₹)*
I. EQUITY AND LIABILITIES			
(1) Shareholder's Funds			
(*a*) Equity Share Capital		10,00,000	10,00,000
(*b*) Reserves and Surplus	1	2,40,000	1,20,000
(2) Non-Current Liabilities			
Long-Term Borrowings — 9% Debentures		3,20,000	2,40,000
(3) Current Liabilities			
(*a*) Trade Payables	2	1,80,000	2,40,000
(*b*) Other Current Liabilities	3	1,80,000	1,60,000
Total		19,20,000	17,60,000
II. ASSETS			
(1) Non-Current Assets			
(*a*) Fixed Assets			
Tangible Assets	4	13,40,000	12,00,000
(*b*) Non-Current Investments	5	2,40,000	1,60,000
(2) Current Assets			
(*a*) Inventories		1,20,000	1,60,000
(*b*) Trade Receivables		1,60,000	1,60,000
(*c*) Cash and Bank Balances		60,000	80,000
Total		19,20,000	17,60,000

Notes to Accounts :

Note No.	Particulars	31-3-2017 (₹)	31-3-2016 (₹)
1.	**Reserves and Surplus :**		
	General Reserve	1,20,000	1,20,000
	Balance in Statement of Profit & Loss	1,20,000	....
		2,40,000	1,20,000
2.	**Trade Payables :**		
	Creditors	1,40,000	1,20,000
	Bills Payable	40,000	1,20,000
		1,80,000	2,40,000
3.	**Other Current Liabilities :**		
	Outstanding Rent	1,80,000	1,60,000
4.	**Tangible Assets :**		
	Plant & Machinery	14,90,000	13,00,000
	Accumulated Depreciation	(1,50,000)	(1,00,000)
		13,40,000	12,00,000
5.	**Non-Current Investments :**		
	Shares in XYZ Limited	2,40,000	1,60,000

Additional Information:

(*a*) During the year 2016-17, a machinery costing ₹50,000 and accumulated depreciation thereon ₹15,000 was sold for ₹32,000.

(*b*) 9 % Debentures ₹80,000 were issued on April 1, 2016.

(C.B.S.E. Sample Paper, 2018)

[Ans. Cash from Operating Activities ₹2,16,800; Cash used in Investing Activities ₹2,88,000; and Cash from Financing Activities ₹51,200.]

Q. 34. Prepare 'Provision for Income Tax Account' from the following informations for preparing Cash Flow Statement :

EQUITY AND LIABILITY SIDE OF BALANCE SHEET

	31-03-2021 ₹	31-03-2022 ₹
Provision for Income Tax	2,20,000	1,90,000

Additional Information :

During the year Income Tax paid was ₹2,30,000

[Ans. Provision made for Income Tax ₹2,00,000.]

Q. 35. Prepare 'Provision for Income Tax Account' from the following informations for preparing Cash Flow Statement :

EQUITY AND LIABILITY SIDE OF BALANCE SHEET

	31-03-2021 ₹	31-03-2022 ₹
Provision for Income Tax	1,50,000	1,34,000

dditional Information :

Provision for Income Tax made during the year 2022 was ₹1,70,000.

[Ans. Income Tax paid ₹1,86,000.]

Q. 36. From the following Balance Sheets of Vivek Ltd., prepare Cash Flow atement :

Particulars	*Note No.*	*31.3.2019*	*31.3.2018*
EQUITY AND LIABILITIES :		₹	₹
(1) Shareholder's Funds :			
(*a*) Share Capital	1	2,90,000	2,50,000
(*b*) Reserve & Surplus		1,52,000	50,000
(2) Current Liabilities :			
(*a*) Trade Payables		5,000	23,000
(*b*) Short term Provision	2	35,000	27,000
TOTAL		4,82,000	3,50,000
ASSETS :			
(1) Non-Current Assets :			
Fixed Assets :			
(*i*) Tangible Assets	3	1,50,000	1,40,000
(*ii*) Intangible Assets		20,000	30,000
(2) Current Assets :			
(*a*) Inventory		95,000	45,000
(*b*) Trade Receivables		2,00,000	1,20,000
(*c*) Cash & Bank Balances		17,000	15,000
TOTAL		4,82,000	3,50,000

otes :	*31.3.2019*	*31.3.2018*
(1) Share Capital :	₹	₹
Equity Share Capital	2,50,000	2,00,000
Preference Share Capital	40,000	50,000
	2,90,000	2,50,000
(2) Short term Provision :		
Provision for Tax	35,000	27,000
(3) Tangible Assets :		
Building	80,000	1,00,000
Plant	70,000	40,000
	1,50,000	1,40,000

itional Information :

(*i*) Depreciation charged on Plant was ₹30,000 and on Building ₹50,000.

(*ii*) Income Tax paid during the year amounted to ₹25,000.

[Ans. Cash from operating activities ₹52,000; Cash used in investing activities ,000; and Cash from financing activities ₹40,000.]

Hint. Provision for Tax made during the year ₹33,000.

Q. 37. From the following Balance Sheets of Tarun Fashions Ltd., prepare a Cash-Flow Statement :—

Particulars	*Note No.*	*31.3.2018*	*31.3.2017*
		₹	₹
I. EQUITY AND LIABILITIES :			
(1) Shareholder's Funds :			
(*a*) Share Capital		1,50,000	1,20,000
(*b*) Reserve and Surplus		1,78,000	75,000
(2) Non-Current Liabilities :			
Long-term Borrowings	1	—	50,000
(3) Current Liabilities :			
(*a*) Trade Payables		31,500	67,000
(*b*) Short term Provisions (Provision for Tax)		42,000	30,000
TOTAL		4,01,500	3,42,000
II. ASSETS :			
(1) Non-Current Assets :			
Fixed Assets :			
(*i*) Tangible Assets	2	2,08,000	1,40,000
(*ii*) Intangible Assets	3	35,000	20,000
(2) Current Assets :			
(*a*) Inventory		1,05,000	1,20,000
(*b*) Trade Receivables		33,500	37,000
(*c*) Cash & Bank Balances		20,000	25,000
TOTAL		4,01,500	3,42,000

Notes : (1) Long-term Borrowing :

	31.3.2018 (₹)	*31.3.2017* (₹)
15% Debentures	—	50,000

(2) Tangible Assets :

Building	80,000	1,00,000
Plant & Machinery	1,28,000	40,000
	2,08,000	1,40,000

(3) Intangible Assets :

Goodwill	35,000	20,000

Additional Information :—

(I) Contingent Liability :

	31.3.2018 (₹)	31.3.2017 (₹)
Proposed Dividend	15,000	12,000

(II) Depreciation of ₹10,000 was provided on Plant & Machinery.

(III) Gain on sale of a part of Building ₹25,000.

(IV) Debentures were redeemed on 1st April, 2017.

(V) Provision for Tax made during the year ₹50,000.

[**Ans.** Cash from operating activities ₹95,000; Cash used in investing activities ₹68,000; and Cash used in financing activities ₹32,000.]

Hint : (1) Increase in Goodwill will be treated as purchase of Goodwill.
(2) Tax paid during the year ₹38,000.

Q. 38. Prepare a Cash-Flow Statement from the following Balance Sheets of Garden Honey Ltd. :—

Particulars	*Note No.*	*31-3-2019*	*31-3-2018*
I. EQUITY AND LIABILITIES :		₹	₹
(1) **Shareholder's Funds :**			
(*a*) Share Capital		2,80,000	2,50,000
(*b*) Reserve and Surplus		1,92,000	1,20,000
(2) **Non-Current Liabilities :**			
Long-term Borrowings	1	—	30,000
(3) **Current Liabilities :**			
(*a*) Short-term Borrowings	2	40,000	70,000
(*b*) Trade Payables		93,000	1,76,000
(*c*) Short term Provision	3	30,000	22,000
TOTAL		6,35,000	6,68,000
II. ASSETS :			
(1) **Non-Current Assets**			
(*a*) Fixed Assets :			
(*i*) Tangible Assets	4	3,65,000	3,50,000
(*ii*) Intangible Assets		42,000	60,000
(*b*) Non-Current Investments		30,000	62,000
(2) **Current Assets :**			
(*a*) Inventory		80,000	1,20,000
(*b*) Trade Receivables		1,00,000	66,000
(*c*) Cash & Bank Balances		18,000	10,000
TOTAL		6,35,000	6,68,000

Notes :	*31.3.2019*	*31.3.2018*
	₹	₹
(1) Long-term Borrowings :		
12% Debentures	—	30,000
(2) Short-term Borrowings :		
Bank Overdraft	40,000	70,000
(3) Short term Provision :		
Provision for Tax	30,000	22,000
(4) Tangible Assets :		
Land & Building	50,000	2,00,000
Plant & Machinery	3,15,000	1,50,000
	3,65,000	3,50,000

Debentures were redeemed on 1st April, 2018.

Additional Information :

(*i*) Depreciation provided during the year was :

On Land & Building	₹12,000
On Plant & Machinery	₹15,000

(*ii*) Land costing ₹80,000 was purchased during the year.

(*iii*) Gain on sale of land was ₹10,000.

[**Ans.** Cash from operating activities ₹38,000; Cash from investing activities Nil and Cash used in financing activities ₹30,000. Sale of Land & Building ₹2,28,000]

Hints : (*i*) Decrease in the amount of Land & Building is treated as sale.
(*ii*) Decrease in Bank Overdraft will be treated as Financing Activity.

Q. 39 (A). Prepare a Cash-Flow Statement from the following Balance Sheets of Dry Fruits Ltd. :—

Particulars	*Note No.*	*31.3.2022*	*31.3.2021*
		₹	₹
I. EQUITY AND LIABILITIES :			
(1) Shareholder's Funds :			
(*a*) Share Capital		2,00,000	2,00,000
(*b*) Reserve and Surplus	1	84,000	(8,000)
(2) Non-Current Liabilities :			
Long-term Borrowings	2	1,35,000	1,00,000
(3) Current Liabilities			
Trade Payables		68,000	62,000
TOTAL		4,87,000	3,54,000
II. ASSETS :			
(1) Non-Current Assets :			
Fixed Assets	3	1,20,000	1,30,000
(2) Current Assets :			
(*a*) Current Investments (Marketable Securities)		22,000	15,000
(*b*) Inventories		61,000	80,000
(*c*) Trade Receivables		40,000	29,000
(*d*) Cash & Bank		2,44,000	1,00,000
TOTAL		4,87,000	3,54,000

Notes : (1) Reserve & Surplus :

	31.3.2022	*31.3.2021*
	₹	₹
General Reserve	24,000	—
Profit & Loss Balance	60,000	(8,000)
	84,000	(8,000)

(2) Long-term Borrowings :

12% Mortgage Loan	1,35,000	1,00,000

(3) Fixed Assets :

Machinery	1,45,000	1,60,000
Less : Accumulated Depreciation	25,000	30,000
	1,20,000	1,30,000

Additional Information :

I. Interest paid on mortgage loan amounted to ₹14,100.

II. Interim Dividend paid during the year ₹20,000.

III. Machinery costing ₹40,000 (accumulated depreciation thereon being ₹18,000) was sold for ₹5,000.

[Ans. Cash from operating activities ₹1,70,100; Cash used in investing activities ₹20,000; and Cash from financing activities ₹900.]

Q. 39 (B). Prepare a Cash-Flow statement from the following :—

Particulars	*Note No.*	*31.3.2022*	*31.3.2021*
I. EQUITY AND LIABILITIES :		₹	₹
(1) Shareholder's Funds :			
(*a*) Share Capital		3,00,000	2,00,000
(*b*) Reserve and Surplus	1	65,000	50,000
(2) Current Liabilities :			
(*a*) Trade Payables	2	1,05,000	52,000
(*b*) Other Current Liabilities	3	—	16,000
(*c*) Short Term Provision	4	20,000	2,000
TOTAL		4,90,000	3,20,000
II. ASSETS :			
(1) Non-Current Assets :			
(*a*) Fixed Assets		2,25,000	1,10,000
(*b*) Non-Current Investments		55,000	60,000
(2) Current Assets :			
(*a*) Inventory		26,000	50,000
(*b*) Trade Receivables		1,80,000	92,000
(*c*) Cash and Bank Balances		4,000	8,000
TOTAL		4,90,000	3,20,000

	31.3.2022	*31.3.2021*
Notes : (1) Reserve & Surplus :	₹	₹
Securities Premium	20,000	—
Profit & Loss Balance	45,000	50,000
	65,000	50,000
(2) Trade Payables :		
Sundry Creditors	95,000	52,000
Bills Payables	10,000	—
	1,05,000	52,000
(3) Other Current Liabilities :		
Outstanding Salaries	—	16,000
(4) Short term Provision :		
Provision for Doubtful Debts	20,000	2,000

Additional Information :—

I. During the year, company sold 60% of its original non-current investments at a profit of 25%.

II. Depreciation provided during the year was ₹35,000.

[**Ans.** Cash from operating activities ₹12,000; Cash used in investing activities ₹1,36,000; and Cash from financing activities ₹1,20,000.]

Q. 40 (A). Prepare a Cash-Flow statement from the following Balance Sheets of ONIDA Ltd. :—

Particulars	*Note No.*	*31.3.2022*	*31.3.2021*
		₹	₹
I. EQUITY AND LIABILITIES :			
(1) Shareholder's Funds :			
(*a*) Share Capital		2,00,000	2,00,000
(*b*) Reserve and Surplus		1,07,000	25,000
(2) Non-Current Liabilities :			
(*a*) Long-term Borrowings	1	1,20,000	—
(3) Current Liabilities :			
(*a*) Trade Payables		1,39,000	90,000
(*b*) Short term Provision	2	40,000	30,000
TOTAL		6,06,000	3,45,000
II. ASSETS :			
(1) Non-Current Assets :			
Fixed Assets :			
(*i*) Tangible Assets		1,80,000	1,20,000
(*ii*) Intangible Assets		34,000	50,000
(2) Current Assets :			
(*a*) Inventory		2,10,000	1,00,000
(*b*) Trade Receivables		1,20,000	50,000
(*c*) Cash & Bank Balances		52,000	13,000
(*d*) Other Current Assets		10,000	12,000
TOTAL		6,06,000	3,45,000

Notes :	*31.3.2022*	*31.3.2021*
	₹	₹
(1) Long-term Borrowings :		
12% Debentures	1,20,000	—
(2) Short term Provision :		
Provision for Taxation	40,000	30,000

Additional Information :—

(I) Debentures were issued on 1st October 2021. Interest has been paid up-to date.

(II) Machinery whose original cost was ₹50,000 (accumulated depreciation thereon being ₹27,000) was sold for ₹35,000.

(III) Depreciation on Machinery charged during the year ₹15,000.

(IV) Interim Dividend paid during the year was @ 15% on Share Capital.

[**Ans.** Cash from operating activities ₹19,200; Cash used in investing activities ₹63,000; and Cash from financing activities ₹82,800.]

Q. 40 (B). From the following Balance Sheets of *X* Ltd., you are required to prepare Cash Flow Statement.

Particulars	Note No.	31.3.2022	31.3.2021
I. EQUITY AND LIABILITIES :		₹	₹
(1) Shareholder's Funds :			
(*a*) Share Capital		8,00,000	6,75,000
(*b*) Reserve and Surplus		1,70,000	91,000
(2) Current Liabilities :			
(*a*) Short-term Borrowings	1	88,000	66,000
(*b*) Trade Payables		1,00,000	70,000
(*c*) Short term Provision	2	34,000	26,000
TOTAL		11,92,000	9,28,000
II. ASSETS :			
(1) Non-Current Assets :			
Fixed Assets	3	3,75,000	5,00,000
(2) Current Assets :			
(*a*) Inventory		4,00,000	2,50,000
(*b*) Trade Receivables		3,82,000	1,55,000
(*c*) Cash & Bank Balances		10,000	3,000
(*d*) Other Current Assets		25,000	20,000
TOTAL		11,92,000	9,28,000

Notes :	31.3.2022	31.3.2021
(1) Short-term Borrowings :	(₹)	(₹)
Bank Overdraft	88,000	66,000
(2) Short term Provision		
Taxation Provision	34,000	26,000
(3) Fixed Assets :		
Land	1,50,000	2,00,000
Plant	2,25,000	3,00,000
	3,75,000	5,00,000

Additional Information :—

(I) Interim Dividend paid during the year ₹60,000.
(II) Land was sold at a profit of ₹30,000.
(III) Plant of the book value of ₹20,000 was sold during the year at a loss of ₹8,000.

[**Ans.** Cash used in operating activities ₹1,72,000; Cash from investing activities ₹92,000; and Cash from financing activities ₹87,000]

Hints. (1) Depreciation on Plant ₹55,000
(2) Increase in Bank Overdraft will be treated as financing activity.

Q. 41. Following are the Balance Sheets of Rashi Ltd. as on 31st March 2022 and 31st March 2021 :

Particulars	Note No.	31.3.2022	31.3.2021
		₹	₹
I. EQUITY AND LIABILITIES :			
(1) Shareholder's Funds :			
(*a*) Share Capital		12,00,000	8,00,000
(*b*) Reserve and Surplus	1	(1,70,000)	(2,15,000)
(2) Non-Current Liabilities :			
Long-term Borrowings	2	3,00,000	2,50,000
(3) Current Liabilities :			
Trade Payables		1,90,000	2,70,000
TOTAL		15,20,000	11,05,000
II. ASSETS :			
(1) Non-Current Assets :			
(*a*) Fixed Assets		6,90,000	5,00,000
(*b*) Non-Current Investments		1,20,000	2,00,000
(2) Current Assets :			
(*a*) Inventory		4,60,000	2,80,000
(*b*) Trade Receivables	3	1,80,000	65,000
(*c*) Cash & Bank Balances		70,000	60,000
TOTAL		15,20,000	11,05,000

Notes :	31.3.2022	31.3.2021
(1) Reserve & Surplus :	₹	₹
Profit & Loss Balance	(1,70,000)	(2,15,000)
(2) Long-term Borrowings		
12% Public Deposits	3,00,000	2,50,000
(3) Trade Receivables :		
Sundry Debtors	1,80,000	50,000
Bills Receivables	—	15,000
	1,80,000	65,000

Additional Information :

(*i*) New public deposits were accepted on 1st January, 2022.

(*ii*) Machinery costing ₹2,00,000 on which depreciation charged was ₹70,000 was sold for ₹1,50,000.

(*iii*) New machinery purchased during the year amounted to ₹4,00,000.

(*iv*) Non-Current Investments were sold at a profit of 25%.

Prepare Cash Flow Statement.

[**Ans.** Cash used in operating activities ₹2,58,500; Cash used in investing activities ₹1,50,000; and Cash from financing activities ₹4,18,500.]

Hints : (1) Depreciation on Plant and Machinery ₹80,000.
(2) Profit as per Balance Sheet ₹2,15,000 – ₹1,70,000 = ₹45,000.
(3) Interest on Public Deposits ₹31,500.

Q. 42. Prepare Cash-Flow Statement from the following Balance Sheets of Mr. Kapoor as on 31st March ....

Liabilities	2018	2019	Assets	2018	2019
	₹	₹		₹	₹
Kapoor's Capital	2,40,000	3,00,000	Fixed Assets	2,00,000	1,60,000
Sundry Creditors	44,000	55,000	Inventory	70,000	55,000
Bills Payable	7,000	10,000	Trade Receivables	30,000	1,20,000
Wages Due	20,000	—	Prepaid Expenses	16,000	10,000
Bank Overdraft	5,000	—	Bank Balance	—	20,000
	3,16,000	3,65,000		3,16,000	3,65,000

Additional Information :—

(*a*) There was neither any drawings nor any capital addition during the year.

(*b*) There was no purchase/sale of fixed assets.

[**Ans.** Cash from operating activities ₹25,000; Cash from investing activities Nil; and Cash used in financing activities ₹5,000.]

Hint. Decrease in Bank Overdraft will be treated as Financing Activity.

Q. 43. Following is the Balance Sheets of Akash Ltd. as at 31-3-2014 :

Akash Ltd.

Balance Sheet *as at 31-3-2014*

	Particulars	Note No.	31.3.2014	31.3.2013
			₹	₹
I	**EQUITY & LIABILITIES**			
	(1) Shareholders' Funds			
	(*a*) Share Capital		15,00,000	14,00,000
	(*b*) Reserves & Surplus	1	2,50,000	1,10,000
	(2) Non-Current Liabilities			
	(*a*) Long Term Borrowings		2,00,000	1,25,000
	(3) Current Liabilities			
	(*a*) Short term borrowings	2	12,000	10,000
	(*b*) Trade Payables		15,000	83,000
	(*c*) Short term provisions	3	18,000	11,000
	TOTAL		19,95,000	17,39,000
II	**(1) Non-Current Assets**			
	(*a*) Fixed Assets			
	(*i*) Tangible assets	4	18,60,000	16,10,000
	(*ii*) Intangible assets	5	50,000	30,000
	(2) Current Assets			
	(*a*) Current Investments		8,000	5,000
	(*b*) Inventories		37,000	59,000
	(*c*) Trade Receivables		26,000	23,000
	(*d*) Cash & Bank		14,000	12,000
	TOTAL		19,95,000	17,39,000

Notes to Accounts :

Note No.	Particulars	31.3.2014 ₹	31.3.2013 ₹
1.	Reserves and Surplus :		
	Surplus (balance in Statement of Profit and Loss)	2,50,000	1,10,000
2.	Short Term Borrowings		
	Bank Overdraft	12,000	10,000
3.	Short term Provisions		
	Provision for Tax	18,000	11,000
4.	Tangible Assets		
	Machinery	20,00,000	17,00,000
	Accumulated Depreciation	(1,40,000)	(90,000)
5.	Intangible Assets		
	Patents	50,000	30,000

Additional Information :

(*i*) Tax paid during the year amounted to ₹16,000.

(*ii*) Machine with a net book value of ₹10,000 (Accumulated Depreciation ₹40,000) was sold for ₹2,000.

Prepare Cash Flow Statement. *(C.B.S.E. Sample Question Paper, 2017)*

[**Ans.** Cash from Operating Activities ₹1,96,000;
Cash used in Investing Activities ₹3,68,000; and
Cash from Financing Activities ₹1,77,000]

Hints :

(*i*) Provision for Tax made during the year ₹23,000.
(*ii*) Net Profit before Tax ₹1,63,000.
(*iii*) Purchase of Machinery ₹3,50,000.

Q. 44. There was 'Nil' net cash flow from operating activities of Ashok Ltd. during the year ending 31st March, 2019. From the following Balance Sheet of Ashok Ltd. as at 31st March, 2019, prepare a Cash Flow Statement :

Ashok Ltd.
Balance Sheet as at 31st March, 2019

Particulars	Note No.	31-3-2019 ₹	31-3-2018 ₹
I. Equity and Liabilities :			
1. **Shareholder's Funds :**			
(*a*) Share Capital		19,00,000	11,00,000
(*b*) Reserves and Surplus	1	1,60,000	2,00,000
2. **Non-current Liabilities :**			
Long term borrowings	2	1,00,000	4,00,000
3. **Current Liabilities :**			
(*a*) Short-term Borrowings	3	2,50,000	2,30,000

(*b*) Short-term Provisions	4	1,90,000	2,70,000
TOTAL		26,00,000	22,00,000
II. Assets :			
1. **Non-current Assets :**			
Fixed Assets :			
(*i*) Tangible Assets	5	15,00,000	11,00,000
(*ii*) Intangible Assets	6	2,80,000	1,70,000
2. **Current Assets :**			
(*a*) Current Investments		1,30,000	2,90,000
(*b*) Trade Receivables		3,90,000	4,10,000
(*c*) Cash at Bank		3,00,000	2,30,000
TOTAL		26,00,000	22,00,000

Notes to Accounts :

Note No.	*Particulars*	*31-3-2019* ₹	*31-3-2018* ₹
1.	**Reserves and Surplus :** Surplus (Balance in Statement of Profit & Loss)	1,60,000	2,00,000
2.	**Long term Borrowings :** 8% Debentures	1,00,000	4,00,000
3.	**Short-term Borrowings :** Bank Overdraft	2,50,000	2,30,000
4.	**Short-term Provisions :** Provision for Tax	1,90,000	2,70,000
5.	**Tangible Assets :**		
	Plant & Machinery	16,30,000	11,70,000
	Accumulated Depreciation	(1,30,000)	(70,000)
		15,00,000	11,00,000
6.	**Intangible Assets :** Goodwill	2,80,000	1,70,000

Additional information :

(*i*) A machinery of the book value of ₹60,000, (depreciation provided thereon ₹20,000) was sold at a loss of ₹6,000.

(*ii*) 8% Debentures were redeemed on 1st July, 2018.

(C.B.S.E. 2020, Rajasthan)

[Ans. Cash used in Investing Activities ₹5,96,000; Cash from Financing Activities ₹5,06,000.]

Hint. Purchase of Plant & Machinery ₹5,40,000

Q. 45. Following is the Balance Sheet of Mevanca Limited as at 31st March, 2017: Prepare Cash Flow Statement when Cash Flow from Financing Activities is ₹2,12,500.

Particulars	Note No.	31.3.2017	31.3.2016
		₹	₹
I. Equity and Liabilities :			
1. Shareholder's Funds			
(a) Share Capital		3,00,000	1,00,000
(b) Reserves and Surplus	1	25,000	1,20,000
2. Non-Current Liabilities			
Long-term Borrowings	2	80,000	60,000
3. Current Liabilities			
(a) Trade Payables		6,000	20,000
(b) Short-term Provisions	3	68,000	70,000
TOTAL		4,79,000	3,70,000
II. Assets :			
1. Non-Current Assets			
Fixed Assets	4	3,36,000	1,92,000
2. Current Assets			
(a) Inventories		67,000	60,000
(b) Trade Receivables		51,000	65,000
(c) Cash and Bank Balances		25,000	49,000
(d) Other Current Assets		—	4,000
TOTAL		4,79,000	3,70,000

Notes to Accounts :

Particulars	31st March 2017	31st March 2016
	₹	₹
1. Reserves and Surplus		
Surplus *i.e.*, Balance in Statement of Profit & Loss	25,000	1,20,000
2. Long-term Borrowings		
10% Long term Loan	80,000	60,000
3. Short-term Provisions		
Provision for Tax	68,000	70,000
4. Fixed Assets :		
Machinery	3,84,000	2,15,000
Accumulated Depreciation	(48,000)	(23,000)
	3,36,000	1,92,000

Additional information :

(*i*) Additional loan was taken on 1st July, 2016.

(*ii*) Tax of ₹53,000 was paid during the year.

(*iii*) Machinery of the book value of ₹80,000 (Accumulated Depreciation ₹20,000) was sold at a loss of ₹18,000.

[**Ans.** Cash used in operating activities ₹29,500; Cash used in Investing Activities ₹2,07,000.]

Hints : (1) Machine with book value of ₹80,000 (Accumulated Depreciation ₹20,000) has been sold. In other words, machine costing ₹1,00,000 has been sold.

(2) Machinery purchased ₹2,69,000; Current year's Depreciation ₹45,000.

Q. 46. From the following information, calculate Cash Flow from Operating Activities :

Particulars	*31st March, 2022 (₹)*	*31st March, 2021 (₹)*
Surplus (*i.e.*, Balance in the Statement for Profit and Loss)	71,000	89,000
Inventory	12,000	4,000
Trade Receivables	58,000	45,000
Outstanding Expenses	14,600	10,000
Goodwill	57,000	27,000
Cash in Hand	9,000	12,000
Machinery	82,000	56,000

(*i*) A piece of machinery costing ₹50,000 on which depreciation of ₹20,000 had been charged was old for ₹10,000. Depreciation charged during the year was ₹18,000.

(*ii*) Income Tax ₹23,000 was paid during the year.

(*iii*) Interim Dividend paid during the year was ₹36,000.

[**Ans.** Cash Flow from Operating Activities ₹39,600.]

Q. 47. Prepare a Cash-Flow Statement from the information given below :—

		₹
Opening Cash Balance		60,000
Closing Cash Balance		35,000
Increase in Trade Receivables		1,50,000
Increase in Trade Payables		90,000
Loss on Sale of Machinery :—	Book Value 80,000	
	Sold for 60,000	20,000
Purchase of Building		3,00,000
Issue of Equity Shares		2,00,000
Preliminary Expenses incurred and Written off		10,000
Net Profit for the year		55,000

[**Ans.** Cash from operating activities ₹25,000; Cash used in investing activities ₹2,40,000; and Cash from financing activities ₹1,90,000.]

Q. 48. The Balance Sheet of *A* Ltd. as at 31-3-2022 and 31-3-2021 were as follows:

Particulars	Note No.	31.3.2022	31.3.2021
		₹	₹
I. EQUITY AND LIABILITIES :			
(1) Shareholder's Funds :			
(*a*) Share Capital		60,000	50,000
(*b*) Reserve and Surplus	1	41,000	46,000
(2) Non-Current Liabilities :			
Long-term Borrowings		25,000	20,000
(3) Current Liabilities :			
(*a*) Trade Payables		12,000	10,000
(*b*) Short term Provision	2	17,000	20,000
TOTAL		1,55,000	1,46,000
II. ASSETS :			
(1) Non-Current Assets :			
(*a*) Fixed Assets		1,00,000	90,000
(2) Current Assets :			
(*a*) Inventory		24,000	20,000
(*b*) Trade Receivables		26,000	32,000
(*c*) Cash & Bank Balances		5,000	4,000
TOTAL		1,55,000	1,46,000

Notes : (1) Reserve & Surplus :	31.3.2022	31.3.2021
	(₹)	(₹)
General Reserve	8,000	5,000
Profit & Loss Balance	33,000	41,000
	41,000	46,000
(2) Short-term Provision :		
Income Tax Provision	17,000	20,000

Additional Information :

(*i*) Depreciation written off on fixed assets was ₹18,000.

(*ii*) Interest paid on Long-term Borrowings amounted to ₹3,000.

(*iii*) Income Tax of ₹15,000 has been paid.

Prepare a Cash-Flow Statement.

[**Ans.** Cash flow from operating activities ₹17,000; Cash used in investing activities ₹28,000; Cash from financing activities ₹12,000; Income Tax provision made ₹12,000.]

Q. 49. The following are the summarised Balance Sheets of *X* Ltd. as at 31st March, 2018 and 2017 :

Particulars	Note No.	31.3.2018	31.3.2017
I. EQUITY AND LIABILITIES :		₹	₹
(1) Shareholder's Funds :			
(*a*) Share Capital		2,50,000	2,00,000
(*b*) Reserve & Surplus		52,000	50,000

(2) Non-Current Liabilities :			
Long-term Borrowings	1	30,000	25,000
(3) Current Liabilities :			
(*a*) Short-term Borrowings	2	7,000	18,000
(*b*) Trade Payables		1,02,000	1,05,000
(*c*) Short term Provisions (Provision for Tax)		24,000	15,000
TOTAL		4,65,000	4,13,000
II. ASSETS :			
(1) Non-Current Assets :			
Fixed Assets	3	1,93,000	2,03,000
(2) Current Assets :			
(*a*) Inventories		1,10,000	90,000
(*b*) Trade Receivables		1,56,000	1,18,000
(*c*) Cash & Bank Balances		6,000	2,000
TOTAL		4,65,000	4,13,000

Notes :		*31.3.2018* (₹)	*31.3.2017* (₹)
(1)	Long-term Borrowings :		
	8% Debentures	30,000	25,000
(2)	Short-term Borrowings :		
	Cash Credit	7,000	18,000
(3)	Fixed Assets	2,50,000	2,40,000
	Less : Accumulated Depreciation	57,000	37,000
		1,93,000	2,03,000

Additional Information :

	31.3.2018 (₹)	*31.3.2017* (₹)
(*i*) Contingent Liability Proposed Dividend	30,000	25,000

(*ii*) Provision for tax made ₹30,000.

(*iii*) Additional debentures amounting to ₹5,000 were issued on 1st Oct. 2017. Interest on debentures has been paid up-to date.

You are required to prepare a statement of Cash-Flow.

[**Ans.** Cash used in operating activities ₹2,800; Cash used in investing activities ₹10,000; and Cash from financing activities ₹16,800; Income Tax paid ₹21,000.]

Note : Repayment of Cash Credit will be treated as 'Financing Activity'.

Q. 50. Prepare a Cash-Flow Statement from the following Balance Sheets of Surya Vanaspati Ltd. :—

Particulars	*Note No.*	*31.3.2022*	*31.3.2021*
		₹	₹
I. EQUITY AND LIABILITIES :			
(1) Shareholder's Funds :			
(*a*) Share Capital		2,50,000	2,00,000
(*b*) Reserve and Surplus		72,000	50,000

(2) Current Liabilities :			
(*a*) Trade Payables		1,13,000	1,30,000
(*b*) Short-term Provision	1	24,000	20,000
TOTAL		4,59,000	4,00,000
II. ASSETS :			
(1) Non-Current Assets :			
Fixed Assets	2	2,52,000	1,50,000
(2) Current Assets :			
(*a*) Inventory		41,000	93,000
(*b*) Trade Receivables	3	1,40,000	1,40,000
(*c*) Other Current Assets	4	6,000	5,000
(*d*) Cash & Bank Balances		20,000	12,000
TOTAL		4,59,000	4,00,000

Notes :	*31-3-2022* (₹)	*31-3-2021* (₹)
(1) Short-term Provision :		
Provision for Taxation	24,000	20,000
(2) Fixed Assets :		
Plant & Machinery	3,00,000	1,90,000
Accumulated Depreciation	(48,000)	(40,000)
	2,52,000	1,50,000
(3) Trade Receivables :		
Sundry Debtors	1,25,000	1,00,000
Bills Receivables	15,000	40,000
	1,40,000	1,40,000
(4) Other Current Assets :		
Prepaid Rent	—	2,000
Prepaid Insurance	6,000	3,000
	6,000	5,000

Additional Information :

(*i*) During the year, machinery whose original cost was ₹50,000 was sold for ₹32,000.

(*ii*) Company charged ₹20,000 as depreciation on Plant and Machinery.

[**Ans.** Cash from operating activities ₹86,000; Cash used in investing activities ₹1,28,000; and Cash from financing activities ₹50,000.]

Hints :

(*i*) Balancing figure of Accumulated Depreciation A/c ₹12,000 being the depreciation on machinery sold will be transferred to the Cr. side of Plant and Machinery A/c.

(*ii*) Loss on sale of Machinery ₹6,000; Purchase of Plant & Machinery ₹1,60,000.

Q. 51. From the following Balance Sheets of *XY* Ltd. prepare a Cash-Flow Statement for the year ended 31st March, 2019 :

Particulars	Note No.	31.3.2019	31.3.2018
I. EQUITY AND LIABILITIES :		₹	₹
(1) **Shareholder's Funds :**			
(*a*) Share Capital		10,00,000	8,00,000
(*b*) Reserve and Surplus	1	6,40,000	5,59,000
(2) **Non-Current Liabilities :**			
Long-term Borrowings	2	1,50,000	1,00,000
(3) **Current Liabilities :**			
Trade Payables		60,000	40,000
TOTAL		18,50,000	14,99,000
II. ASSETS :			
(1) **Non-Current Assets :**			
(*a*) Fixed Assets :			
(*i*) Tangible Assets		7,50,000	5,10,000
(*ii*) Intangible Assets		15,000	20,000
(*b*) Non-Current Investments	3	1,00,000	30,000
(2) **Current Assets :**			
(*a*) Inventory		6,30,000	4,20,000
(*b*) Trade Receivables		3,20,000	4,94,000
(*c*) Cash & Bank Balances		28,000	20,000
(*d*) Other Current Assets	4	7,000	5,000
TOTAL		18,50,000	14,99,000

Notes : (1) Reserve & Surplus :

	31.3.2019	31.3.2018
	₹	₹
General Reserve	5,20,000	4,00,000
Profit & Loss Balance	1,20,000	1,59,000
	6,40,000	5,59,000

(2) Long-term Borrowings :

8% Debentures	1,50,000	1,00,000

(3) Rate of Interest on Non-Current Investment is 10% p.a.

(4) Other Current Assets :

Prepaid Expenses	4,000	—
Accrued Income	3,000	5,000
	7,000	5,000

Additional Information :

(*i*) Depreciation of ₹30,000 has been charged on machinery.

(*ii*) Non-Current Investments costing ₹30,000 were sold for ₹40,000 at the end of the year.

(*iii*) New debentures were issued on 1st October, 2018.

(*iv*) During the year share issue expenses amounted to ₹10,000 and these were written off from Statement of Profit & Loss.

[**Ans.** Cash from operating activities ₹1,05,000; Cash used in Investing Activities ₹3,27,000; and Cash from Financing Activities ₹2,30,000]

Note : It has been assumed that non-current investments have been purchased at the end of the accounting year, *i.e.*, on 31st March, 2019.

Q. 52. You are required to prepare a Cash Flow Statement (as per AS-3) for the year 2021-22 from the following Balance Sheets :

BALANCE SHEET OF A.B.C. LTD.

As at 31st March, 2022 and 31st March, 2021

Particulars	*Note No.*	*31.03.2022*	*31.03.2021*
I. EQUITY AND LIABILITIES :		₹	₹
1. Shareholder's Funds :			
(*a*) Share Capital (Equity Share Capital)		6,00,000	4,00,000
(*b*) Reserves and Surplus (Statement of P/L)		2,00,000	1,00,000
2. Non-Current Liabilities :			
(*a*) Long-term Borrowings		1,00,000	2,00,000
3. Current Liabilities :			
(*a*) Short-term borrowings (Bank loan)		—	10,000
(*b*) Trade Payables (Creditors)		1,05,000	1,40,000
(*c*) Short-term Provisions (Provision for Tax)		70,000	40,000
TOTAL		10,75,000	8,90,000
II. ASSETS :			
1. Non-Current Assets :			
(*a*) Fixed Assets			
(*i*) Tangible (Building)		6,00,000	6,00,000
(*ii*) Intangible (Patents)		45,000	50,000
(*b*) Non-Current Investments		75,000	—
2. Current Assets :			
(*a*) Inventories		15,000	10,000
(*b*) Trade Receivables (Debtors)		2,55,000	2,00,000
(*c*) Cash and Bank Balances		85,000	30,000
TOTAL		10,75,000	8,90,000

Additional Information :

During the year 2021-22 :

(*i*) Building costing ₹75,000 was purchased.

(*ii*) An old building, the book value of which was ₹63,000, was sold at a loss of ₹5,000.

(*iii*) Tax provided during the year was ₹80,000.

(*iv*) Proposed Dividend for the year ended 31st March, 2021 was 20% and for the year ended 31st March, 2022 was 10%. *(I.S.C. 2015, Modified)*

[**Ans.** Cash Flow from Operating Activities ₹1,37,000; Cash used in Investing Activities ₹92,000; Cash Flow from Financing Activities ₹10,000]

Hint. Depreciation on Building ascertained by preparing Building A/c ₹12,000.

Q. 53. Given below are the Balance Sheets of *X* Ltd. as at 31st March, 2019 and 31st March, 2018.

Particulars	*Note No.*	*31st March, 2019*	*31st March, 2018*
I. EQUITY AND LIABILITIES :		₹	₹
1. Shareholder's Funds :			
(*a*) Equity Share Capital		3,50,000	3,00,000
(*b*) Reserves and Surplus	1	2,20,000	1,60,000
2. Non-Current Liabilities :			
Long-term Borrowings	2	2,50,000	1,50,000
3. Current Liabilities :			
Trade Payables	3	1,25,000	85,000
TOTAL		9,45,000	6,95,000
II. ASSETS :			
1. Non-Current Assets :			
(*a*) Fixed Assets :			
(*i*) Tangible Assets (Machinery)		4,10,000	3,20,000
(*ii*) Intangible Assets (Goodwill)		80,000	1,00,000
(*b*) Non-current Investments	4	80,000	30,000
2. Current Assets :			
(*a*) Inventories		55,000	40,000
(*b*) Trade Receivables		1,90,000	80,000
(*c*) Cash and Bank Balances	5	1,30,000	1,25,000
TOTAL		9,45,000	6,95,000

Notes to Accounts :

Particulars	*31st March, 2019*	*31st March, 2018*
	₹	₹
1. Reserves and Surplus		
General Reserve	1,45,000	1,00,000
Surplus, *i.e.*, Balance in Statement of Profit and Loss	75,000	60,000
	2,20,000	1,60,000
2. Long-term Borrowings		
11% Debentures	2,50,000	1,50,000
3. Trade Payables		
Creditors	1,10,000	75,000
Bills Payable	15,000	10,000
	1,25,000	85,000
4. Non-Current Investments		
12% Investments	80,000	30,000

5. Cash and Bank Balances	1,30,000	1,20,000
Bank	—	5,000
Cash	1,30,000	1,25,000

Additional Information :

1. Investments costing ₹30,000 were sold for ₹36,000 at the end of the year.
2. New debentures have been issued at the end of the current accounting year at a discount of 5% which was written off from General Reserve.
3. New investments have been purchased at the end of the current accounting year.
4. Depreciation charged on Machinery during the current accounting year was ₹10,000.

From the above information, prepare Cash Flow Statement as per Accountin Standard-3 (Revised). *(I.S.C. 2011, Modified)*

[**Ans.** Cash from Operating Activities ₹16,900; Cash used in Investing Activitie ₹1,40,400; Cash from Financing Activities ₹1,28,500.]

ADDITIONAL QUESTIONS

(For Practice)

Q. 54. Calculate Cash Flow from Investing Activities from the followin information :

(*i*) Machinery costing ₹5,00,000 (Book Value ₹3,50,000) was sold at a loss 10%.

(*ii*) Dividend received @10% from Long term Investments of ₹2,00,000.

(*iii*) Receipt for permission granted for use of Trade Mark ₹1,20,000.

(*iv*) Non-Current Investments purchased ₹1,75,000.

(*v*) Non-Current Investment costing ₹3,00,000 was sold at a profit of 20%.

(*vi*) Land was sold for ₹6,00,000 of which 40% is profit.

[**Ans.** Net Cash Inflow from Investing Activities ₹12,40,000.]

Q. 55. Prepare a Cash-Flow Statement from the Balance Sheets given below :—

Particulars	*Note No.*	*31.3.2022*	*31.3.202*
I. EQUITY AND LIABILITIES :		₹	₹
(1) Shareholder's Funds :			
(*a*) Share Capital		5,00,000	5,00,00
(*b*) Reserve and Surplus	1	2,25,000	90,00
(2) Non-Current Liabilities :			
Long-term Borrowings	2	25,000	—
(3) Current Liabilities :			
(*a*) Trade Payables		1,00,000	80,00
(*b*) Short-term Provision	3	15,000	20,00
TOTAL		8,65,000	6,90,00

II. ASSETS :			
(1) **Non-Current Assets**			
Fixed Assets		3,10,000	3,00,000
(2) **Current Assets :**			
(*a*) Current Investments (Marketable)		16,000	20,000
(*b*) Inventory		3,20,000	1,50,000
(*c*) Trade Receivables		2,00,000	2,10,000
(*d*) Cash & Bank		19,000	10,000
TOTAL		8,65,000	6,90,000

Notes :	31.3.2022	31.3.2021
	₹	₹
(1) Reserve & Surplus :		
General Reserve	1,50,000	1,20,000
Profit & Loss Balance	75,000	(30,000)
	2,25,000	90,000
(2) Long-term Borrowings :		
Mortgage Loan	25,000	—
(3) Short-term Provision :		
Income Tax Provision	15,000	20,000

Additional Information :—

(*i*) Depreciation written off on fixed assets @ 10% on last year's balance.
(*ii*) Interim Dividend paid during the year @ 10% on Share Capital.
(*iii*) Mortgage Loan was taken on 1st July 2021 @ 10% p.a. Interest has been paid up-to date.

[Ans. Cash from operating activities ₹71,875; Cash used in investing activities ₹40,000; and Cash used in financing activities ₹26,875.]

Q. 56. Following are the Balance Sheets of *X* Ltd. :—

Particulars	Note No.	31.3.2022	31.3.2021
		₹	₹
I. EQUITY AND LIABILITIES :			
(1) **Shareholder's Funds :**			
(*a*) Share Capital		2,00,000	2,00,000
(*b*) Reserve and Surplus	1	72,000	(37,000)
(2) **Non-Current Liabilities :**			
Long-term Borrowings	2	75,000	50,000
(3) **Current Liabilities :**			
(*a*) Trade Payables		44,000	46,000
(*b*) Short-term Provision	3	24,000	30,000
TOTAL		4,15,000	2,89,000
II. ASSETS :			
(1) **Non-Current Assets :**			
(*a*) Fixed Assets	4	62,000	1,40,000
(*b*) Non-Current Investments		2,000	10,000
(2) **Current Assets :**			
(*a*) Inventory		2,00,000	60,000

(*b*) Trade Receivables	1,21,000	56,000
(*c*) Cash & Bank Balances	30,000	23,000
TOTAL	4,15,000	2,89,000

Notes :		31.3.2022	31.3.2021
		₹	₹
(1)	Reserve & Surplus :		
	General Reserve	22,000	—
	Profit & Loss Balance	50,000	(37,000)
		72,000	(37,000)
(2)	Long-term Borrowings :		
	Public Deposits	75,000	50,000
(3)	Short-term Provision :		
	Provision for Taxation	20,000	25,000
	Provision for Doubtful Debts	4,000	5,000
		24,000	30,000
(4)	Fixed Assets :		
	Land	—	1,00,000
	Plant & Machinery	1,00,000	80,000
	Accumulated Depreciation	(38,000)	(40,000)
		62,000	1,40,000

Additional Information :—

(I) A piece of machinery was sold for ₹8,000 during the year 2022. Its original cost was ₹20,000 and depreciation of ₹15,000 has been provided on it.

(II) Investments were sold at a loss of 40%.

(III) Land was sold for ₹1,50,000.

(IV) Interest paid on public deposits amounted to ₹6,000.

You are required to prepare Cash-Flow Statement.

[Ans. Cash used (lost) in operating activities ₹1,34,800; Cash from investing activities ₹1,22,800; and Cash from financing activities ₹19,000.

Hint : Non-Current Investments costing ₹8,000 are sold for ₹4,800.

Q. 57. From the following Balance Sheets of Godrej Ltd., you are required to prepare Cash-Flow Statement.

Particulars	Note No.	31.3.2022	31.3.2021
I. EQUITY AND LIABILITIES :		₹	₹
(1) Shareholder's Funds :			
(*a*) Share Capital		3,30,000	3,00,000
(*b*) Reserve & Surplus		25,000	30,000
(2) Non-Current Liabilities :			
Long-term Borrowings		25,000	40,000
(3) Current Liabilities :			
(*a*) Short-term Borrowings	1	5,000	—

(*b*) Trade Payables		97,000	1,24,000
(*c*) Short-term Provision	2	30,000	24,000
TOTAL		5,12,000	5,18,000
II. ASSETS :			
(1) Non-Current Assets :			
(*a*) Fixed Assets :			
(*i*) Tangible Assets		2,60,000	2,00,000
(*ii*) Intangible Assets	3	7,500	60,000
(*b*) Non-Current Investments		64,000	50,000
(2) Current Assets :			
(*a*) Inventory		62,500	70,000
(*b*) Trade Receivables		98,000	1,30,000
(*c*) Cash & Bank Balances		20,000	8,000
TOTAL		5,12,000	5,18,000

Notes :	31.3.2022	31.3.2021
	₹	₹
(1) Short-term Borrowings :		
Bank Overdraft	5,000	—
(2) Short-term Provision :		
Taxation Provision	30,000	24,000
(3) Intangible Assets :		
Goodwill	—	50,000
Patents	7,500	10,000
	7,500	60,000

Additional Information :—

(I) Machinery whose original cost was ₹50,000 (accumulated depreciation thereon being ₹32,000) was sold for ₹10,000.

(II) Depreciation on Machinery charged during the year was ₹25,000.

(III) Non-Current Investments costing ₹20,000 were sold for ₹32,000 during the year.

(IV) Interest paid on long-term borrowings amounted to ₹3,000.

[Ans. Cash from operating activities ₹90,000; Cash used in investing activities ₹95,000; Cash from financing activities ₹17,000. Purchase of Tangible Fixed Assets ₹1,03,000.

Notes : (1) Patents are assumed to be written off.
(2) Bank Overdraft is treated as financing activity.

Q. 58. Following are the Balance Sheets of Pawan Ltd. :—

Particulars	*Note No.*	*31.3.2022*	*31.3.2021*
		₹	₹
I. EQUITY AND LIABILITIES :			
(1) Shareholder's Funds :			
(*a*) Share Capital		3,00,000	2,50,000
(*b*) Reserve and Surplus	1	2,07,000	1,75,000

(2) Current Liabilities :			
(*a*) Short-term Borrowings	2	20,000	15,000
(*b*) Trade Payables		31,000	54,000
(*c*) Short-term Provision	3	84,000	81,000
TOTAL		6,42,000	5,75,000
II. ASSETS :			
(1) Non-Current Assets :			
(*a*) Fixed Assets :			
(*i*) Tangible Assets	4	2,70,000	2,70,000
(*ii*) Intangible Assets		50,000	30,000
(*b*) Non-Current Investments		45,000	50,000
(2) Current Assets :			
(*a*) Trade Receivables		2,67,000	2,19,000
(*b*) Cash & Bank Balances		10,000	6,000
TOTAL		6,42,000	5,75,000

Notes : (1)	*31.3.2022*	*31.3.2021*
	₹	₹
Reserve & Surplus	1,97,000	1,75,000
Securities Premium Reserve	10,000	—
	2,07,000	1,75,000
(2) Short-term Borrowings :		
Bank Overdraft	20,000	15,000
(3) Short-term Provision :		
Provision for Tax	62,000	65,000
Provision for Doubtful Debts	22,000	16,000
	84,000	81,000
(4) Tangible Assets :		
Land	1,50,000	70,000
Machinery	1,20,000	2,00,000
	2,70,000	2,70,000

(I) Machinery of the book value of ₹60,000 was sold for ₹18,000 during the year.

(II) Interim Dividend paid during the year ₹25,000.

(III) During the year Company sold 40% of its original non-current investments a a loss of 20%.

You are required to prepare Cash-Flow Statement.

[**Ans.** Cash from operating activities ₹45,000; Cash used in investing activities ₹81,000; and Cash from financing activities ₹40,000.]

Hints : (1) Current year's Depreciation ₹20,000.

(2) Purchase of Non-Current Investments ₹15,000.

(3) Increase in Intangible Assets will be treated as purchase of Intangible Assets.

Q. 59. Following are the Balance Sheets of 'X' Co. Ltd. :—

Particulars	Note No.	31.3.2022	31.3.2021
I. EQUITY AND LIABILITIES :		₹	₹
(1) **Shareholder's Funds :**			
Share Capital		3,00,000	2,50,000
(2) **Non-Current Liabilities :**			
Long-term Borrowings	1	45,000	80,000
(3) **Current Liabilities :**			
Trade Payables		42,500	28,000
TOTAL		3,87,500	3,58,000
II. ASSETS :			
(1) **Non-Current Assets :**			
(*a*) Fixed Assets :			
(*i*) Tangible Assets	2	3,02,500	2,70,000
(2) **Current Assets :**			
(*a*) Inventory		25,000	45,000
(*b*) Trade Receivables		50,000	35,000
(*c*) Cash & Bank Balances		10,000	8,000
TOTAL		3,87,500	3,58,000

Notes :	31.3.2022	31.3.2021
(1) Long-term Borrowings :	(₹)	(₹)
Loan from Bank	45,000	80,000
(2) Tangible Fixed Assets :		
Land and Building	2,20,000	1,50,000
Machinery	82,500	1,20,000
	3,02,500	2,70,000

A machine costing ₹40,000 having book value of ₹25,000 was sold for ₹35,000 during the year. Interest paid on loan from bank amounted to ₹8,000. Prepare a Cash-Flow Statement.

[Ans. Cash from operating activities ₹30,000; Cash used in investing activities ₹35,000; and Cash from financing activities ₹7,000.]

Q. 60. You are required to prepare Cash-Flow Statement from the following informations :—

	₹
(*i*) Interim Dividend paid during the year	7,000
(*ii*) Plant Purchased	20,000
(*iii*) Intangible Assets written off during the year	10,000
(*iv*) Debentures redeemed on 1st Feb. 2022	12,000

(*v*) Interest on debentures has been paid up-to date.

BALANCE SHEET

as at 31st March 2022 and 2021

Particulars	*Note No.*	*31.3.2022* ₹	*31.3.2021* ₹
I. EQUITY AND LIABILITIES :			
(1) Shareholder's Funds :			
(*a*) Share Capital		1,48,000	1,40,000
(*b*) Reserve & Surplus		21,120	20,080
(2) Non-Current Liabilities :			
Long-term Borrowings	1	12,000	24,000
(3) Current Liabilities :			
(*a*) Trade Payables		23,680	20,720
(*b*) Short Term Provision	2	1,600	1,400
TOTAL		2,06,400	2,06,200
II. ASSETS :			
(1) Non-Current Assets :			
Fixed Assets :			
(*i*) Tangible Assets		60,000	40,000
(*ii*) Intangible Assets		10,000	20,000
(2) Current Assets :			
(*a*) Inventory		85,400	98,400
(*b*) Trade Receivables		35,400	29,800
(*c*) Cash & Bank Balances		15,600	18,000
TOTAL		2,06,400	2,06,200

Notes : (1)	*31.3.2022* (₹)	*31.3.2021* (₹)
Long-term Borrowings :		
12% Debentures	12,000	24,000
(2) Short Term Provision :		
Provision for Doubtful Debts	1,600	1,400

[Ans. Cash from operating activities ₹31,240; Cash used in investing activities ₹20,000; and Cash used in financing activities ₹13,640.]

Q. 61. From the following information, prepare a Cash-Flow Statement :—

	₹
Opening Cash Balance	10,000
Closing Cash Balance	12,000
Decrease in Trade Receivables	5,000
Increase in Trade Payables	7,000
Sale of fixed assets	20,000
Redemption of Debentures	50,000
Net Profit for the year	20,000

[Ans. Cash from operating activities ₹32,000; Cash from investing activities ₹20,000; and Cash used in financing activities ₹50,000.]

Q. 62. From the following informations, prepare a Cash-Flow Statement :

	₹
Increase in Equity Share Capital	40,000
Interim Dividend paid during the year	17,500
Transfer to General Reserve	2,000
Purchase of Building	33,250

Additional Information :—

	31-3-2021 ₹	31-3-2022 ₹
Cash at Bank	25,000	37,500
Trade Receivables	75,000	90,000
Trade Payables	50,000	37,500
Outstanding Wages	22,500	16,250
Profit & Loss Balance	42,000	79,500

[**Ans.** Cash from operating activities ₹23,250; Cash used in investing activities ₹33,250; and Cash from financing activities ₹22,500]

Q. 63. From the following extracts of a company's Balance Sheets, calculate for the year ending 31st March, 2022 :

(*i*) Cash from investing activities.

(*ii*) Cash from financing activities.

(**Note :** *Current year's figures appear in the first column and the previous year's figures are in the second column.*)

Particulars	*31.3.2022* ₹	*31.3.2021* ₹
Equity Share Capital	13,00,000	12,00,000
Long Term Borrowing (10% Bank Loan)	60,000	1,00,000
Dividend Payable	3,000	—
Fixed assets :		
Plant and Machinery	1,70,000	1,40,000
Less : Accumulated Depreciation	(24,000)	(40,500)
Non-current investments	1,00,000	20,000
Land (at cost)	5,00,000	7,00,000
Goodwill	30,000	40,000

Additional information :

	31.3.2022	*31.3.2021*
(*i*) **Contingent Liability :** Proposed Dividend (₹)	20,000	21,000

(*ii*) The Loan instalment and interest on loan was paid at the end of the financial year.

(*iii*) During the year 2021-22 :

(*a*) The company provided depreciation on Plant and Machinery amounting to ₹13,500.

(*b*) The company sold 70% of its non-current investments which it held at the beginning of the year, at a profit of 20% on its book value.

(I.S.C. 2014 Modified)

SOLUTION : CASH FLOW FROM INVESTING ACTIVITIES

Particulars	₹
Purchase of Plant and Machinery⁽¹⁾	(60,000)
Sale of Non-Current Investments	16,800
Purchase of Non-Current Investments⁽³⁾	(94,000)
Sale of Land	2,00,000
Net Cash Flow from Investing Activities	62,800

CASH FLOW FROM FINANCING ACTIVITIES

Particulars	₹
Proceeds from Issue of Equity Shares	1,00,000
Repayment of Bank Loan	(40,000)
Interest paid on Bank Loan (10% of ₹1,00,000)	(10,000)
Payment of Proposed Dividend (₹21,000 – Dividend Payable ₹3,000)	(18,000)
Net Cash Flow from Financing Activities	32,000

Working Notes :

(1)

Dr. PLANT & MACHINERY ACCOUNT Cr.

Particulars	₹	*Particulars*	₹
To Balance b/d	1,40,000	By Accumulated Depreciation A/c*	30,000
To Bank A/c (Balancing figure, being purchase)	60,000	By Balance c/d	1,70,000
	2,00,000		2,00,000

(2)

Dr. ACCUMULATED DEPRECIATION ACCOUNT Cr.

Particulars	₹	*Particulars*	₹
To Plant & Machinery A/c*	30,000	By Balance b/d	40,500
To Balance c/d	24,000	By Statement of Profit & Loss (Current Year's Depreciation)	13,500
	54,000		54,000

*Balancing figure represents fully depreciated Plant & Machinery written off.

(3)

NON-CURRENT INVESTMENTS ACCOUNT

Dr. Cr.

Particulars	₹	*Particulars*	₹
To Balance b/d	20,000	By Bank A/c (Sale)(4)	16,800
To Gain on Sale	2,800	By Balance c/d	1,00,000
To Bank A/c (Balancing figure, being purchase)	94,000		
	1,16,800		1,16,800

(4)	₹
70% of Investments at the beginning of the year : 70% of ₹20,000 =	14,000
Add : 20% profit on ₹14,000	2,800
Sale price of Investments	16,800

Q. 64. From the following extracts of a company's Balance Sheets, calculate Cash from Financing Activities for the year ending 31st March, 2022 :

Particulars	*31.3.2022*	*31.3.2021*
	₹	₹
Equity Share Capital	9,00,000	7,00,000
Securities Premium Reserve	1,25,000	1,00,000
12% Debentures	4,00,000	3,00,000
Bank Overdraft	12,000	10,000

Additional information :

	31.3.2022	*31.3.2021*
(*i*) **Contingent Liability :** Proposed Dividend (₹)	60,000	70,000

(*ii*) Debentures were issued on 1st April, 2021, at a discount of 10%.

(*iii*) Unclaimed Dividend ₹7,000. *(ISC Sample Paper, 2017 Modified)*

SOLUTION : CASH FLOW FROM FINANCING ACTIVITIES

Particulars	₹
Proceeds from Issue of Equity Shares	2,00,000
Proceeds from Securities Premium	25,000
Issue of Debentures (₹1,00,000 *less* Discount ₹10,000)	90,000
Interest paid on Debentures (12% on ₹4,00,000)	(48,000)
Payment of Proposed Dividend (Note 1)	(63,000)
Increase in Bank Overdraft	2,000
Net Cash Flows from Financing Activities	2,06,000

Working Note (1) :

	₹
Proposed Dividend for 31.3.2021	70,000
Less : Unclaimed Dividend	7,000
Payment made	63,000

Q. 65. From the following information of Purity Ltd., calculate :

(*i*) Cash from Operating Activities.

(*ii*) Cash from Financing Activities.

Particulars	31-03-2022	31-03-2021
	₹	₹
Trade Receivables	17,000	20,000
Inventories	25,000	30,000
Prepaid Expenses	12,000	10,000
Expenses Outstanding	9,000	7,000
Provision for Tax	15,000	10,000
Cash in Hand	50,000	75,000
Furniture (at book value)	1,20,000	1,60,000
General Reserve	50,000	40,000
10% Debentures	40,000	30,000
Goodwill	60,000	70,000
Trade Payables	21,000	25,000
Balance of Profit and Loss (Cr.)	1,30,000	1,20,000
Share Capital	5,00,000	3,00,000

Additional Information :

	31.3.2022	31.3.2021
(*a*) **Contingent Liability :** Proposed Dividend (₹)	5,000	4,000

(*b*) A piece of furniture costing ₹30,000 (accumulated depreciation ₹3,000) was sold for ₹25,000.

(*c*) Tax of ₹9,000 was paid.

(*d*) Interim Dividend of ₹4,000 was paid.

(*e*) The company paid ₹3,000 as interest on debentures. *(I.S.C. 2017 modified)*

SOLUTION :

(*i*) CASH FLOW FROM OPERATING ACTIVITIES

Particulars		₹	₹
Net Profit before Tax (Note 3)		42,000	
Adjustment for non-cash and non-operating items :			
Add : Goodwill Written off		10,000	
Depreciation on Furniture (Note 1)		13,000	
Loss on Sale of Furniture		2,000	
Interest on Debentures		3,000	
Operating Profit before Working Capital Changes		70,000	
Add : Decrease in Current Assets :			
Trade Receivables	3,000		
Inventories	5,000		
Increase in Current Liabilities :			
Expenses Outstanding	2,000	10,000	
		80,000	

Less : Increase in Current Assets :			
Prepaid Expenses	2,000		
Decrease in Current Liabilities :			
Trade Payables	4,000	6,000	
		74,000	
Less : Payment of Tax		9,000	
Cash Flow from Operating Activities		65,000	65,000

Working Notes :

(1)

Dr. **FURNITURE ACCOUNT** Cr.

Particulars	₹	*Particulars*	₹
To Balance b/d	1,60,000	By Bank A/c (Sale)	25,000
		By Statement of P & L (Loss on Sale) (₹30,000 – ₹3,000 – ₹25,000)	2,000
		By Depreciation (Balancing Figure)	13,000
		By Balance c/d	1,20,000
	1,60,000		1,60,000

(2)

Dr. **PROVISION FOR TAX ACCOUNT** Cr.

Particulars	₹	*Particulars*	₹
To Bank	9,000	By Balance b/d	10,000
To Balance c/d	15,000	By Statement of Profit & Loss (Balancing figure, being provision made)	14,000
	24,000		24,000

(3) Calculation of Net Profit before Tax :

		₹
Profit & Loss Balance on 31st March 2022		1,30,000
Less : Profit & Loss Balance on 31st March 2021		1,20,000
		10,000
Add : Transfer to General Reserve	10,000	
Interim Dividend Paid	4,000	
Proposed Dividend for 2021	4,000	
Provision for Tax (Note 2)	14,000	32,000
Net Profit before Tax		42,000

(*ii*) Cash Flow from Financing Activities :

Particulars	₹	₹
Issue of Share Capital	2,00,000	
Issue of Debentures	10,000	

Payment of Interest on Debentures	(3,000)	
Interim Dividend Paid	(4,000)	
Proposed Dividend Paid (for 2021)	(4,000)	
Cash Flow from Financing Activities	1,99,000	1,99,000

Q. 66. From the following statement, calculate Cash from Operating Activities :

STATEMENT OF PROFIT AND LOSS

for the year ending 31st March, 2018

Particulars	*Note No.*	₹
Revenue from operations		1,00,000
Other Income	1	10,000
Total Revenue		1,10,000
Expenses :		
Employee Benefit Expenses		10,000
Depreciation and Amortization Expenses	2	28,000
Finance Cost (Interest on Debentures)		5,000
Other Expenses	3	12,000
Total Expenses		55,000
Profit before Tax		55,000
Less : Provision for Tax		(27,000)
Profit after Tax		28,000

Notes to Accounts :

Particulars	₹
1. **Other Income**	
Profit on sale of Land and Building	6,000
Interest on investments (including interest accrued ₹1,000)	4,000
	10,000
2. **Depreciation and Amortization Expenses :**	
Depreciation on Land and Building	18,000
Amortization of Patents	10,000
	28,000
3. **Other Expenses**	
Commission (including outstanding commission ₹5,000)	6,000
Carriage inward	6,000
	12,000

Additional Information :

(1) During the year 2017-18, tax paid was ₹25,000.

(2) Proposed Dividend for the year ended 31st March, 2018 was ₹15,000.

(I.S.C. Specimen Question Paper 2018)

SOLUTION:

CASH FLOW FROM OPERATING ACTIVITIES

for the year ended 31st March, 2018

Particulars	₹	₹
Net Profit before Tax		55,000
Adjustment for Non-Cash and Non-Operating Items :		
Depreciation on Land and Building	18,000	
Amortisation of Patents	10,000	
Interest on Debentures	5,000	33,000
		88,000
Less : Profit on sale of Land and Building	6,000	
Interest on Investments	4,000	10,000
Operating Profit before Working Capital Changes		78,000
Add : Increase in Current Liabilities		
Outstanding Commission		5,000
		83,000
Less : Increase in Current Assets		
Interest Accrued		1,000
Cash Generated from Operating Activities		82,000
Less : Tax Paid		25,000
Net Cash Flow from Operating Activities		57,000

Q. 67. From the following information and extracts of Balance Sheets of Pioneer Ltd. as at 31st March, 2017 and 31st March, 2018, calculate for the year 2017-18 :

(*i*) Cash Flow from Operating Activities

(*ii*) Cash Flow from Investing Activities

Particulars	*31.3.2018* ₹	31.3.2017 ₹
General Reserve	40,000	30,000
Balance in Statement of Profit and Loss	2,40,000	1,40,000
Provision for Tax	1,20,000	90,000
Trade Payables	32,000	44,000
Plant and Machinery (at cost)	2,90,000	2,45,000
Accumulated depreciation on Plant and Machinery	30,000	40,000
Patents	50,000	1,50,000
10% Debentures	1,20,000	10,000
Goodwill	15,000	12,000

Note : Proposed dividends for the years 2016-17 and 2017-18 were ₹40,000 and ₹50,000 respectively.

Additional Information :

During the year 2017-18 :

(*a*) The company provided depreciation on Plant and Machinery amounting to ₹24,000.

(*b*) A fully depreciated machine had been condemned and scrapped.

(*c*) Some patents were written off while some patents were sold for ₹75,000 at a profit of ₹5,000. No new patents were purchased.

(*d*) Interest of ₹12,000 was paid on Debentures.

(*e*) Tax paid ₹50,000.

(*f*) Dividend proposed in 2016-17 was approved by the shareholders and paid by the company. (*I.S.C. 2019*)

SOLUTION : Cash Flow from Operating Activities

Particulars	₹
Net Profit before Tax (Working Note)	2,30,000
Add : Non-operating/non-cash expenses	
Interest on Debentures	12,000
Depreciation on Plant and Machinery	24,000
Amortization of Patents	30,000
	2,96,000
Less : Non-Operating/Non-Cash gains	
Gain on sale of Patents	(5,000)
Net operating profit before working capital changes	2,91,000
Less : Decrease in Trade Payables	(12,000)
Cash from Operating Activities before Tax	2,79,000
Less : Tax Paid	(50,000)
Cash from Operating Activities	2,29,000

Cash Flow from Investing Activities

Particulars	₹
Purchase of Plant & Machinery	(79,000)
Purchase of Goodwill	(3,000)
Sale of Patents	75,000
Cash used in Investing Activities	(7,000)

Working Notes :

Dr. Plant & Machinery Account Cr.

Particulars	₹	*Particulars*	₹
To Balance b/d	2,45,000	By Accumulated Dep. (Machine condemned transferred from Acc. Dep. A/c)	34,000
To Bank A/c (Purchase of Machinery)	79,000	By Balance c/d	2,90,000
	3,24,000		3,24,000

Dr. Accumulated Depreciation Account Cr.

Particulars	₹	*Particulars*	₹
To Plant & Machinery (Bal. Fig. being machine condemned transferred to Plant & Machinery A/c)	34,000	By Balance b/d	40,000
		By Depreciation A/c	24,000

To Balance c/d	30,000		
	64,000		64,000

Dr. **Patents Account** Cr.

Particulars	₹	Particulars	₹
To Balance b/d	1,50,000	By Bank A/c	75,000
To Gain on Sale	5,000	By Statement of P & L (Patents written off) (Bal. Fig.)	30,000
		By Balance c/d	50,000
	1,55,000		1,55,000

Dr. **Provision for Tax Account** Cr.

Particulars	₹	Particulars	₹
To Bank A/c	50,000	By Balance b/d	90,000
To Balance c/d	1,20,000	By Statement of P & L	80,000
	1,70,000		1,70,000

Calculation of Net Profit before Tax :

Particulars	₹
Net Profit for the year	1,00,000
Add : Transfer to General Reserve	10,000
Add : Proposed Dividend of 2016-17	40,000
Add : Provision for Tax	80,000
Net Profit before Tax	2,30,000

Q. 68 From the following extract of the Balance Sheet of Regal Ltd., taking into consideration the additional information, you are required to calculate the amounts of the following items to be shown in the company's Cash Flow Statement for the year 2018-19 :

(*i*) Fixed asset purchased.
(*ii*) Fixed asset sold.
(*iii*) Profit/Loss on sale of fixed asset.
(*iv*) Depreciation charged on fixed assets.

Particulars	31.03.2019 (₹)	31.03.2018 (₹)
Fixed Asset	6,00,000	4,90,000

Additional information :

(*i*) The provision for depreciation on fixed assets stood at ₹1,40,000 on 31st March, 2018 and ₹1,80,000 on 31st March, 2019.

(*ii*) During the year 2018-19, a fixed asset costing ₹60,000 (book value ₹30,000) was sold for ₹20,000. *(I.S.C. 2020)*

SOLUTION:

Since provision for depreciation is given in additional information, fixed assets stated in the question must be at book values and not on original cost.

(1)

Dr. FIXED ASSET ACCOUNT (On Written Down Value) Cr.

Particulars	₹	*Particulars*	₹
To Balance b/d	4,90,000	By Bank A/c (Sale)	20,000
To Bank A/c (Balancing figure, being purchase)	2,10,000	By Loss on Sale	10,000
		By Depreciation A/c (As per Note 2)	70,000
		By Balance c/d	6,00,000
	7,00,000		7,00,000

(2)

Dr. PROVISION FOR DEPRECIATION ACCOUNT Cr.

Particulars	₹	*Particulars*	₹
To Fixed Asset A/c (Accumulated Dep. on Asset sold)	30,000	By Balance b/d	1,40,000
To Balance c/d	1,80,000	By Depreciation A/c (Balancing figure, being current years' depreciation)	70,000
	2,10,000		2,10,000

In case, Fixed Asset A/c is prepared on the basis of Original Cost, it will appear as follows :

Dr. FIXED ASSET ACCOUNT (On Original Cost) Cr.

Particulars	₹	*Particulars*	₹
To Balance b/d (4,90,000 + 1,40,000)	6,30,000	By Bank A/c (Sale)	20,000
To Bank A/c (Balancing figure, being purchase)	2,10,000	By Loss on Sale	10,000
		By Provision for Depreciation A/c	30,000
		By Balance c/d (6,00,000 + 1,80,000)	7,80,000
	8,40,000		8,40,000

(*i*) Fixed assets purchased are of ₹2,10,000 (Note 1)

(*ii*) Fixed assets are sold for ₹20,000.

(*iii*) Loss on sale of fixed assets is ₹10,000 (Note 1).

(*iv*) Depreciation charged on fixed assets is ₹70,000.

Q. 69. You are required to prepare a Cash-Flow Statement (as per AS-3) for the year 2018-19 from the following Balance Sheets :

BALANCE SHEET OF HILLOCK LTD.

as at 31st March, 2018 and 31st March 2019

Particulars	*Note No.*	*31.3.2019*	*31.3.2018*
I. EQUITY AND LIABILITIES :			
1. **Shareholder's Funds :**		₹	₹
(*a*) Equity Share Capital		2,50,000	2,00,000
(*b*) Reserve and Surplus	1	90,000	50,000
2. **Current Liabilities :**			
(*a*) Short-term Borrowings (Bank overdraft)		—	10,000
(*b*) Trade Payables		20,000	15,000
(*c*) Other Current Liabilities	2	5,000	5,000
(*d*) Short-term Provisions (Provision for Tax)		25,000	20,000
Total		3,90,000	3,00,000
II. ASSETS :			
1. **Non-Current Assets :**			
Fixed Assets – Tangible		2,55,000	2,35,000
2. **Current Assets :**			
(*a*) Current Investments		30,000	—
(*b*) Inventories		15,000	25,000
(*c*) Trade Receivables		40,000	10,000
(*d*) Cash and Bank Balances		50,000	30,000
Total		3,90,000	3,00,000

Notes to Accounts :

	31.3.2019	*31.3.2018*
(1) Reserves and Surplus		
Balance in Statement of Profit and Loss	70,000	40,000
Securities Premium Reserve	20,000	10,000
	90,000	50,000
(2) Other Current Liabilities		
Outstanding Expenses	1,000	5,000
Unclaimed Dividend	4,000	—
	5,000	5,000
(3) Contingent Liability :		
Proposed Dividend	5,000	10,000

Additional Information :

During the year 2018-19 :

(*i*) A tangible fixed asset costing ₹50,000 was purchased.

(*ii*) Tax paid ₹15,000.

(*iii*) Interest of ₹1,000 was paid on the bank overdraft. *(I.S.C. 2020)*

SOLUTION: CASH FLOW STATEMENT OF HILLOCK LTD.

for the year ending 31st March, 2019

Particulars		₹	₹
A. Cash Flow from Operating Activities :			
Net Profit before Tax (Working Note 1)		60,000	
Add : Non-Cash and Non Operating Items			
Depreciation on Plant & Machinery	30,000		
Interest on Bank Overdraft	1,000	31,000	
		91,000	
Operating Profit before Working Capital changes			
Add : Increase in Trade Payables	5,000		
Decrease in Inventories	10,000	15,000	
		1,06,000	
Less : Increase in Trade Receivables	30,000		
Increase in Current Investments	30,000		
Decrease in Outstanding Expenses	4,000	64,000	
Cash Flow from Operating Activities before Tax paid		42,000	
Less : Tax paid		(15,000)	
Cash flow from Operating Activities			27,000
B. Cash Flow from Investing Activities :			
Purchase of Fixed Asset		(50,000)	
Cash used in Investing Activities			(50,000)
C. Cash Flow from Financing Activities :			
Issue of Share Capital		50,000	
Security Premium Reserve received on issue of share capital		10,000	
Bank Overdraft repaid		(10,000)	
Interest paid on bank Overdraft		(1,000)	
Dividend paid (for 31st March, 2018)		(6,000)	
Cash Flow from Financing Activities			43,000
Net Increase in Cash and Cash Equivalents			20,000
Add : Opening Cash and Cash Equivalents			30,000
Closing Cash and Cash Equivalents			50,000

Working Notes :

	₹
(1) Net Profit for the year (₹70,000 – ₹40,000)	30,000
Add : Dividend declared (Proposed Dividend for 31st March 2018)	10,000
Add : Provision for Tax for Current year (Note 2)	20,000
Net Profit before Tax	60,000

(2)

Dr. FIXED ASSETS ACCOUNT Cr.

Particulars	₹	*Particulars*	₹
To Balance b/d	2,35,000	By Depreciation A/c	30,000
To Bank A/c	50,000	By Balance c/d	2,55,000
	2,85,000		2,85,000

(3)

Dr. PROVISION FOR TAX ACCOUNT Cr.

Particulars	₹	Particulars	₹
To Bank A/c (Tax Paid)	15,000	By Balance b/d	20,000
To Balance c/d	25,000	By Statement of Profit & Loss (Current year's Provision)	20,000
	40,000		40,000

Multiple Choice Questions

Choose the Best Alternative

Q. 1. Cash flow statement is prepared for financial planning of ______

(A) Long range
(B) Medium range
(C) Short range
(D) Very Long range

Q. 2. Which of the following is source of cash?

(A) Cash deposited into Bank
(B) Cash withdrawn from Bank
(C) Sale of Goods costing ₹10,000 for ₹8,000
(D) Sale of marketable securities for cash

Q. 3. Which of the following is not source of cash?

(A) Issue of shares
(B) Purchase of Machinery
(C) Sale of Asset
(D) Dividend received

Q. 4. Which of the following is not application of cash?

(A) Increase in Debtors
(B) Increase in Inventory
(C) Increase in Bills Payable
(D) Increase in Prepaid Expenses

Q. 5. Cash from operating activities consists of

(A) Operating Profit
(B) Decrease/Increase in Current Assets
(C) Decrease/Increase in Current Assets
(D) All of the Above

Q. 6. While calculating operating profit which will be added to net profit

(A) Preliminary Expenses Written off
(B) Depreciation
(C) Loss on Sale of Asset
(D) All of the Above

Q. 7. While calculating operating profit which will be added to net profit

(A) Profit on Sale of Asset
(B) Increase in General Reserves
(C) Interest received
(D) Refund of Tax

Q. 8. While calculating cash flow from operating activities which will be deducted

(A) Decrease in Prepaid Expenses
(B) Increase in Trade Payables
(C) Increase in Trade Receivables
(D) Decrease in Trade Receivables

Q. 9. While calculating cash flow from operating activities which will be added :

(A) Increase in Inventory (B) Increase in Creditors
(C) Decrease in Bills Payable (D) Increase in Trade Receivables

Q. 10. Cash from Operating activities will decrease due to :

(A) Increase in Current Assets (B) Decrease in Current Liabilities
(C) Neither of the two (D) Both A and B above

Q. 11. Which of the following is incorrect about the statement of cash flows?

(A) It provides information about the cash receipt and cash payments of an enterprise.
(B) It reconciles ending cash balance with the balance as per bank statement.
(C) It provides information about the operating, investing and financing activities.
(D) It explains the deviation of cash from Earnings.

Q. 12. The statement of cash flows clarifies cash flows according to ....

(A) Operating and non-operating flows
(B) Investing and non-operating flows
(C) Inflows and outflows
(D) Operating, investing and financing activities

. 13. An example of cash flow from operating activity is :

(A) Purchase of own debenture
(B) Sale of fixed assets
(C) Interest paid on term-deposits by a bank
(D) Issue of equity share capital

14. An example of Cash Flow from Operating Activity is :

(A) Cash receipts from sale of goods and services
(B) Sale of long-term investments
(C) Interest Received
(D) Issue of Debentures

15. Which of the following is an example of cash flow from Operating Activities?

(A) Issue of Shares
(B) Purchase of Machinery
(C) Purchase of Investment
(D) Purchase of Inventory for Cash

16. An example of cash flow from investing activity is :

(A) Issue of debenture
(B) Repayment of long-term loan
(C) Purchase of raw materials for cash
(D) Sale of investment by non-financial enterprise.

Q. 17. An example of Cash Flows from Investing Activity is :

(A) Cash Revenue from Operations

(B) Commission Received

(C) Payment of cash for purchase of fixed assets

(D) Dividend paid

Q. 18. An Example of cash flow from financing activity is :

(A) Payment of dividend
(B) Receipt of dividend on investment
(C) Cash received from customer
(D) Purchase of fixed asset

Q. 19. An example of Cash Flows from Financing Activity is :

(A) Credit Revenue from Operations
(B) Cash receipts from issue of shares
(C) Sale of Investments
(D) Interest Received

Q. 20. Paid ₹4,00,000 to acquire shares in R.Y. Ltd. and received a dividend of ₹40,000 after acquisition. These transactions will result in :

(A) Cash used in investing activities ₹4,00,000.

(B) Cash generated from financing activities ₹4,40,000.

(C) Cash used in investing activities ₹3,60,000.

(D) Cash generated from financing activities ₹3,60,000.

(C.B.S.E. 2020, Rajasthan)

Q. 21. If a machine whose original cost is ₹40,000 having accumulated depreciation ₹12,000, were sold for ₹34,000 then while preparing Cash Flow Statement its effect on cash flow will be :

(A) Cash flow from financing activities	₹34,000
(B) Cash flow from financing activities	₹ 6,000
(C) Cash flow from investing activities	₹34,000
(D) Cash flow from investing activities	₹ 6,000

Q. 22. If 6% Pref. share capital ₹2,00,000 were redeemed at a premium of 5%, while preparing Cash Flow Statement its effect on cash flow will be :

(A) Cash used from financing activities	₹2,12,000
(B) Cash received from financing activities	₹2,12,000
(C) Cash used (Payment) from financial activities	₹2,10,000
(D) Cash used (Payment) from financial activities	₹2,00,000

Q. 23. If the amount of goodwill is ₹40,000 at the beginning of a year and ₹48,000 at the end of that year then while preparing cash flow statement its effect on cash flow will be :

(A) Cash used (Payment) in Investing Activities	₹8,000
(B) Cash received from operating activities	₹8,000
(C) Cash used (Payment) from Operating Activities	₹8,000
(D) Cash used (Payment) from Financial Activities	₹8,000

Q. 24. How will you deal increase in the balance of 'Securities Premium Reserve' while preparing a Cash Flow Statement?

(A) Cash Flow from Operating Activities
(B) Cash Flow from Investing Activities
(C) Cash Flow from Financing Activities
(D) Cash Equivalent

Q. 25. Fine Garments Ltd. is engaged in the export of readymade garments. The company purchased a machinery of ₹10,00,000 for the use in packaging of such garments. Cash flow due to the purchase of machinery will be cash flow from :

(A) Cash Flow from Operating Activities
(B) Cash Flow from Investing Activities
(C) Cash Flow from Financing Activities
(D) Cash Equivalent

Q. 26. A Ltd., engaged in the business of retailing of two wheelers, invested ₹ 50,00,000 in the shares of a manufacturing company. Dividend received on this investment will be :

(A) Cash Flow from Operating Activities
(B) Cash Flow from Investing Activities
(C) Cash Flow from Financing Activities
(D) Cash Equivalent

Q. 27. How will you treat payment of dividend in a Cash flow statement?

(A) Cash Flow from Operating Activities
(B) Cash Flow from Investing Activities
(C) Cash Flow from Financing Activities
(D) Cash Equivalent

Q. 28. How will you treat Bank Overdraft in a Cash Flow Statement?

(A) Cash Flow from Operating Activities
(B) Cash Flow from Investing Activities
(C) Cash Flow from Financing Activities
(D) Cash Equivalent

Q. 29. Where will you show purchase of Goodwill in a Cash Flow Statement?

(A) Cash Flow from Operating Activities
(B) Cash Flow from Investing Activities
(C) Cash Flow from Financing Activities
(D) Cash Equivalent

Q. 30. How will you treat payment of 'Interest on Debentures' while preparing a Cash Flow Statement?

(A) Cash Flow from Operating Activities
(B) Cash Flow from Investing Activities
(C) Cash Flow from Financing Activities
(D) Cash Equivalent

Q. 31. Interest received by a finance company is classified under which kind of activity while preparing a Cash flow statement?

(A) Cash Flow from Operating Activities
(B) Cash Flow from Investing Activities
(C) Cash Flow from Financing Activities
(D) No Cash Flow

Q. 32. State whether cash deposited in bank will be classified under which kind of activity?

(A) Cash Flow from Operating Activities
(B) Cash Flow from Investing Activities
(C) Cash Flow from Financing Activities
(D) No Cash Flow

Q. 33. Mention the net amount of 'Source' or 'Use' of cash when a fixed asset having book value of ₹15,000 is sold at a loss of ₹5,000.

(A) Use ₹5,000 (B) Source ₹10,000
(C) Use ₹15,000 (D) Source ₹15,000

Q. 34. Dividend paid by a Trading company is classified under which kind of activity while preparing cash flow statement?

(A) Cash Flow from Operating Activities
(B) Cash Flow from Investing Activities
(C) Cash Flow from Financing Activities
(D) No Cash Flow

Q. 35. A company receives a dividend of ₹2 Lakhs on its investment in other company's shares. In case of a Finance Company, it will be classified under which kind of activity?

(A) Cash Flow from Operating Activities
(B) Cash Flow from Investing Activities
(C) Cash Flow from Financing Activities
(D) No Cash Flow

Q. 36. How will you classify loans given by Tata Finance Company?

(A) Cash Flow from Operating Activities
(B) Cash Flow from Investing Activities
(C) Cash Flow from Financing Activities
(D) No Cash Flow

Q. 37. How will you classify deposits by customers in Axis Bank?

(A) Cash Flow from Operating Activities
(B) Cash Flow from Investing Activities
(C) Cash Flow from Financing Activities
(D) No Cash Flow

Q. 38. A Mutual Fund Company receives a dividend of ₹20 Lakhs on its investments in another company's shares. Where will it appear in a Cash Flow Statement?

(A) Cash Flow from Operating Activities
(B) Cash Flow from Investing Activities
(C) Cash Flow from Financing Activities
(D) No Cash Flow

Q. 39. Dividend paid by a finance company is classified under which kind of activity while preparing cash flow statement?
(A) Cash Flow from Operating Activities
(B) Cash Flow from Investing Activities
(C) Cash Flow from Financing Activities
(D) No Cash Flow

Q. 40 Dividend paid by a manufacturing company is classified under which kind of activity while preparing cash flow statement?
(A) Cash Flow from Operating Activities
(B) Cash Flow from Investing Activities
(C) Cash Flow from Financing Activities
(D) No Cash Flow

Q. 41. Interest paid by an investment company will come under which kind of activity while preparing cash flow statement?
(A) Cash Flow from Operating Activities
(B) Cash Flow from Investing Activities
(C) Cash Flow from Financing Activities
(D) No Cash Flow

Q. 42. Which of the following item is not considered as Cash Equivalents?
(A) Short term Deposits in Bank (B) Commercial Papers
(C) Treasury Bills (D) Investment

Q. 43. Which of the following item is considered as Cash Equivalents?
(A) Marketable Securities (B) Debtors
(C) Investment (D) Bills of Exchange

Q. 44. Which of the following is considered as Cash Equivalents?
(A) Bank deposits for 2 months (B) Commercial Papers
(C) Treasury Bills (D) All of the above

Q. 45. Cash deposit with the bank with a maturity date after two months belongs to which of the following in the cash flow statement :
(A) Investing activities (B) Financing activities
(C) Cash and Cash equivalents (D) Operating activities

(C.B.S.E. Sample Paper, 2015)

Q. 46. Issue of Debentures for consideration other than cash is shown under which activity?
(A) Operating Activity (B) Investing Activity
(C) Financing Activity (D) None of the above

Q. 47. An Investment normally qualifies as cash-equivalent only when from the date of acquisition it has a short maturity period of :

(A) One month or less (B) Three months or less

(C) Three months or more (D) One year or less

(C.B.S.E. 2020, Mumbai, Chennai)

Q. 48. *X* Ltd. purchased furniture for ₹20,00,000 paying 60% by issue of equity shares of ₹10 each and the balance by a cheque. This transaction will result in :

(A) Cash used in investing activities ₹20,00,000.

(B) Cash generated from financing activities ₹12,00,000.

(C) Increase in cash and cash equivalents ₹8,00,000.

(D) Cash used in investing activities ₹8,00,000.

(C.B.S.E. 2020, Kolkata, Lucknow)

Q. 49. Balance Sheet (Extract)

Equity and Liabilities	*31-3-2019*	*31-3-2020*
	₹	₹
12% Debentures	2,00,000	1,60,000

Additionl Information :

Interest on debentures is paid on half yearly basis on 30th September and 31st March each year.

Debentures were redeemed on 30th September 2019.

How much amount (related to above information) will be shown in Financing Activity for Cash Flow Statement prepared on 31st March 2020?

(A) Outflow ₹40,000 (B) Inflow ₹42,600

(C) Outflow ₹61,600 (D) Outflow ₹64,000

(C.B.S.E. Sample Paper, 2020)

Q. 50. Which of the following is not an investing activity under cash flow statement?

(A) Purchase of marketable securities for ₹25,000 for cash.

(B) Sale of land for ₹28,000 for cash.

(C) Sale of 2,500 shares (held as investment) for ₹15 each.

(D) Purchase of equipment for ₹500 for cash.

(C.B.S.E. Sample Paper, 2020)

(See Answers at the end of the book.)

14

Ratio Analysis

Absolute figures expressed in monetary terms in financial statements by themselves are meaningless. These figures often do not convey much meaning unless expressed in relation to other figures.

For example, one trader Mr. Anil earns a profit of ₹1,50,000, whereas another trader Mr. Sunil earns a profit of ₹1,80,000. Which one of them is more efficient? Generally we can say that Sunil is more efficient as he is earning more profits. But in order to give the correct answer, we must find out, how much the capital is employed by each of them. Suppose, Anil has employed a capital of ₹10,00,000 and Sunil has employed ₹15,00,000, we can now calculate the percentage of profit earned by each of them on the capital employed :

$$\text{Anil} = \frac{1{,}50{,}000}{10{,}00{,}000} \times 100 = 15\%$$

$$\text{Sunil} = \frac{1{,}80{,}000}{15{,}00{,}000} \times 100 = 12\%$$

This shows that Anil has earned ₹15 for every ₹100 of capital, whereas Sunil has earned ₹12 for every ₹100 of capital. As such, Anil is using his capital more efficiently.

The above example shows that figures assume significance only when expressed in relation to other figures. Just as in the example given above, the absolute figure of profit was meaningless but when the figure of profit was expressed in relation to capital, it assumed significance.

Meaning of Ratio : Relationship between two figures, expressed in arithmetical terms is called a 'ratio'. In the words of R. N. Anthony :

"A Ratio is simply one number expressed in terms of another. It is found by dividing one number into the other."

Ratio may be expressed in the following four ways :

(1) **'Proportion' or Pure Ratio or Simple Ratio :**— It is expressed by the simple division of one number by another. For example, if the current assets of a business are ₹2,00,000 and its current liabilities are ₹1,00,000, the ratio of 'Current assets to current liabilities' will be 2 : 1.

(2) **'Rate' or 'So Many Times' :**— In this type, it is calculated how many times a figure is, in comparison to another figure. For example, if a firm's credit sales during the year are ₹2,00,000 and its debtors at the end of the year are ₹40,000, its Debtors Turnover Ratio $= \frac{2{,}00{,}000}{40{,}000} = 5$ times. It shows that the credit sales are 5 times in comparison to debtors.

(3) **Percentage** :— In this type, the relation between two figures is expressed in hundredth. For example, if a firm's capital is ₹10,00,000 and its profit is ₹2,00,000, the ratio of profit to capital, in terms of percentage, is $\frac{2,00,000}{10,00,000} \times 100 = 20\%$.

(4) **Fraction** :— Say, net profit is one-fifth of capital.

While calculating a ratio, it should be understood that it is desirable to divide the "more favourable figure" by the "less favourable figure".

Objectives of Ratio Analysis :

(*i*) To locate the weak spots of business which need more attention.

(*ii*) To provide deeper analysis of the liquidity, solvency, activity and profitability of the business.

(*iii*) To provide information for making cross-sectional analysis *i.e.* for making comparison with that of some selected firms in the same industry.

(*iv*) To provide information for making time-series analysis *i.e.* for making comparison of a firm's present ratios with its past ratios.

(*v*) To provide information useful for making estimates and preparing the plans for the future.

Advantages or Uses of Accounting Ratios

Financial statements, *i.e.*, Profit and Loss Statement and Balance Sheet prepared at the end of the year do not always convey to the reader the real profitability and financial health of the business. They contain various facts and figures and it is for the reader to conclude, whether these facts indicate a good or bad managerial performance. Ratio analysis is the most important tool of analysing these financial statements. It helps the reader in giving tongue to the mute heaps of figures given in financial statements. The figures then speak of liquidity, solvency, profitability etc. of the business enterprise. Some important advantages derived by a firm by the use of accounting ratios are :—

(1) **Helpful in Analysis of Financial Statements** :— Ratio analysis is an extremely useful device for analysing the financial statements. It helps the bankers, creditors, investors, shareholders etc. in acquiring enough knowledge about the profitability and financial health of the business. In the light of the knowledge so acquired by them, they can take necessary decisions about their relationships with the concern.

(2) **Simplification of Accounting Data** :— Accounting ratio simplifies and summarises a long array of accounting data and makes them understandable. It discloses the relationship between two such figures which have a cause and effect relationship with each other.

(3) **Helpful in Comparative Study** :— With the help of ratio analysis comparison of profitability and financial soundness can be made between one firm and another in the same industry. Similarly, comparison of current year figures can also be made with those of previous years with the help of ratio analysis.

(4) **Helpful in Locating the Weak Spots of the Business** :— Current year's ratios are compared with those of the previous years and if some weak spots are thus located, remedial measures are taken to correct them.

(5) **Helpful in Forecasting :—** Accounting ratios are very helpful in forecasting and preparing the plans for the future. For example, if revenue from operations (sales) of a firm during this year are ₹10 Lakhs and the average amount of inventory kept during the year was ₹2 Lakhs, *i.e.*, 20% of sales and if the firm wishes to increase sales next year to ₹15 Lakhs, it must be ready to keep an inventory of ₹3,00,000, *i.e.*, 20% of 15 Lakhs. Similar other estimates for future can be worked out by establishing a relationship between capital and revenue from operations; debtors and revenue from operations; expenses and revenue from operations etc.

(6) **Estimate about the Trend of the Business :—** If accounting ratios are prepared for a number of years, they will reveal the trend of costs, revenue from operations, profits and other important facts.

(7) **Fixation of Ideal Standards :—** Ratios help us in establishing ideal standards of the different items of the business. By comparing the actual ratios calculated at the end of the year with the ideal ratios, the efficiency of the business can be easily measured.

(8) **Effective Control :—** Ratio analysis discloses the liquidity, solvency and profitability of the business enterprise. Such information enables management to assess the changes that have taken place over a period of time in the financial activities of the business. It helps them in discharging their managerial functions, *e.g.*, planning, organising, directing, communicating and controlling more effectively.

(9) **Study of Financial Soundness :—** Ratio analysis discloses the position of business with different view-points. It discloses the position of business with the liquidity point of view, solvency point of view, profitability point of view etc. With the help of such a study we can draw conclusions regarding the financial health of the business enterprise.

Limitations of Accounting Ratios

Accounting ratios are very important tool of financial analysis. But despite its being indispensable, the ratios suffer from a number of limitations. These limitations should be kept in mind while making use of accounting ratios :

(1) **False Accounting Data Gives False Ratios :—** Accounting ratios are calculated on the basis of data given in profit and loss statement and balance sheet. Therefore, they will be only as correct as the accounting data on which they are based. For example, if closing inventory is over-valued, not only the profitability will be overstated but also the financial position will appear to be better. Therefore, unless the profit and loss statement and balance sheet are reliable, the ratios based on them will not be reliable. There are certain limitations of financial statements, as discussed in the previous chapter, as such, the ratios calculated on the basis of such financial statements will also have the same limitations.

(2) **Comparison not Possible if Different Firms Adopt Different Accounting Policies :—** There may be different accounting policies adopted by different firms with regard to providing depreciation, creation of provision for doubtful debts, method of valuation of closing inventory etc. For instance, one firm may adopt the policy of charging depreciation on straight-line basis, while other may charge on written-down value method. Such differences make the accounting ratios incomparable.

(3) **Ratio Analysis Becomes Less Effective Due to Price Level Changes** :— Price level over the years goes on changing, therefore, the ratios of various years cannot be compared. For example, one firm sells 1,000 Machines for ₹10 Lakhs during 2021; it again sells 1,000 Machines of the same type in 2022 but owing to rising prices the sale price was ₹15 Lakhs. On the basis of ratios it will be concluded that the sales have increased by 50%, whereas in actual, sales have not increased at all. Hence, the figures of the past years must be adjusted in the light of price level changes before the ratios for these years are compared.

(4) **Ratios may be Misleading in the Absence of Absolute Data** :— For example, *X* company produces 10 Lakh metres of cloth in 2021 and 15 Lakh metres in 2022, the progress is 50%. *Y* company raises its production from 10 thousand metres in 2021 to 20 thousand metres in 2022, the progress is 100%. Comparison of these two firms made on the basis of ratio will disclose that the second firm is more active than the first firm. Such conclusion is quite misleading because of the difference in the size of the two firms. It is, therefore, essential to study the ratios along with the absolute data on which they are based.

(5) **Limited Use of a Single Ratio** :— The analyst should not merely rely on a single ratio. He should study several connected ratios before reaching a conclusion. For example, the **Current Ratio** of a firm may be quite satisfactory, whereas the **Quick Ratio** may be unsatisfactory.

(6) **Window-Dressing** :– Some companies in order to cover up their bad financial position resort to window dressing *i.e.*, showing a better position than the one which really exists. They change their balance sheet in such a way that the important facts and truth may be concealed. For example, the current assets of a company are ₹2,00,000 and its current liabilities are ₹1,00,000, so the current ratio is 2 : 1. After this, it purchased goods for ₹1,00,000 for credit in the month of March. If it records the purchases, the current assets will increase to ₹3,00,000 and current liabilities will increase to ₹2,00,000. As a result, the current ratio will be reduced to 3 : 2 or 1.5 : 1. The company may pass the entry for purchase in the beginning of the next year or may postpone the purchase itself for a few days more.

(7) **Lack of Proper Standards** :— Circumstances differ from firm to firm hence no single standard ratio can be fixed for all the firms against which the actual ratio may be compared. For example, the current ratio of 2 : 1 is generally accepted as an ideal ratio, which means that the current assets should be at least twice in comparison to the current liabilities. But if a firm has such type of arrangement with its bankers that the bankers will provide necessary credit to the firm in case of need, the ideal current ratio for such a firm may be less than 2 : 1.

(8) **Ignores Qualitative Factors** :— Ratio analysis is a quantitative measurement of the performance of the business. It ignores qualitative factors which are also essential for interpretation. For example, credit may be granted to a customer on the basis of certain ratios of his business but the character and managerial ability of the customer must also be taken into consideration.

(9) **Ratios Alone are not Adequate for Proper Conclusions** :— Ratios derived from analysis of statements are not sure indicators of good or bad financial position and profitability of a firm. They merely indicate the probability of favourable or unfavourable position. The analyst has to carry out further investigations and exercise

his judgement in arriving at a correct diagnosis. This is for this reason that an analyst has to use other tools of financial analysis in addition to the tool of ratio analysis.

(10) **Effect of Personal Ability and Bias of the Analyst :—** Another important point to keep in mind is that different persons draw different meaning of different terms. One analyst may calculate ratios on the basis of profit after interest and tax, whereas another analyst may consider profits before interest and tax, a third may consider profits after interest but before tax. Therefore, before making comparisons, one must be sure that the ratios have been calculated on the same basis.

Although ratio analysis suffers from a number of limitations as enumerated above, yet it is a very useful and widely used tool of analysing the financial statements. Useful conclusions may be arrived at by ratio analysis provided the above-mentioned limitations are kept in mind while using the results obtained from ratio analysis.

Classification of Ratios

Ratios may be classified in several ways. One classification is based on the statement from where the figures are drawn. On this basis the ratios may be classified as follows :

(*a*) **Balance Sheet Ratios** *i.e.*, ratios computed on the basis of figures drawn from the Balance Sheet. These ratios consist of the following ratios :

(*i*) Current Ratio
(*ii*) Quick Ratio
(*iii*) Debt-equity Ratio
(*iv*) Debt to Total Assets Ratio
(*v*) Proprietary Ratio

(*b*) **Statement of Profit & Loss Ratios :** i.e., ratios computed on the basis of figures drawn from the Statement of Profit and Loss. These ratios consist of the following ratios :

(*i*) Gross Profit Ratio
(*ii*) Net Profit Ratio
(*iii*) Operating Ratio
(*iv*) Operating Profit Ratio
(*v*) Interest Coverage Ratio

(*c*) **Composite Ratios,** *i.e.*, ratios computed on the basis of figures drawn from both Statement of Profit and Loss and Balance Sheet. These ratios consist of the following ratios :

(*i*) Trade Receivables Turnover Ratio
(*ii*) Trade Payables Turnover Ratio
(*iii*) Working Capital Turnover Ratio
(*iv*) Inventory Turnover Ratio
(*v*) Earning Per Share
(*vi*) Price Earning Ratio
(*vii*) Return on Investment

However, the above classification is unsuitable from the users point of view. Users of financial statements *i.e.*, short-term creditors, long-term creditors, shareholders etc. are interested in knowing the liquidity, solvency, activity and profitability of the enterprise. On this basis ratios may be classified into the four categories as follows :

(A) Liquidity Ratios
(B) Solvency Ratios
(C) Activity or Turnover Ratios
(D) Profitability Ratios or Income Ratios

(A) **Liquidity Ratios :—** "Liquidity" refers to the ability of the firm to meet its current liabilities. The liquidity ratios, therefore, are also called 'Short-term Solvency Ratios.' These ratios are used to assess the short-term financial position of the concern. They indicate the firm's ability to meet its current obligations out of current resources.

In the words of Saloman J. Flink, "Liquidity is the ability of the firm to meet its current obligations as they fall due."

In the words of Herbert B. Mayo, "Liquidity is the ease with which assets may be converted into cash without loss."

Short-term creditors of the firm are primarily interested in the liquidity ratios of the firm as they want to know how promptly or readily the firm can meet its current liabilities. If the firm wants to take a short-term loan from the bank, the bankers also study the liquidity ratios of the firm in order to assess the margin between current assets and current liabilities.

Liquidity ratios include two ratios :—

(*i*) Current Ratio or Working Capital Ratio
(*ii*) Quick Ratio or Acid Test Ratio or Liquid Ratio

(B) **Solvency Ratios :—** These ratios are calculated to assess the ability of the firm to meet its long-term liabilities as and when they become due. These ratios reveal as to how much amount in a business has been invested by proprietors and how much amount has been raised from outside sources. Solvency ratios disclose the firm's ability to meet the interest costs regularly and long-term indebtedness at maturity. Some important solvency ratios are :—

(*i*) Debt Equity Ratio
(*ii*) Debt to Total Assets Ratio
(*iii*) Proprietary Ratio
(*iv*) Interest Coverage Ratio

(C) **Activity Ratios :—** These ratios are calculated on the basis of 'cost of sales' or 'sales', therefore, these ratios are also called as 'Turnover Ratios'. Turnover indicates the speed or number of times the capital employed has been rotated in the process of doing business. In other words, these ratios indicate how efficiently the working capital and inventory is being used to obtain sales. Higher turnover ratios indicate the better use of capital or resources and in turn lead to higher profitability. Some important turnover ratios are :—

(*i*) Inventory Turnover Ratio
(*ii*) Trade Receivables Turnover Ratio
(*iii*) Trade Payables Turnover Ratio
(*iv*) Working Capital Turnover Ratio

(D) **Profitability Ratios or Income Ratios :—** The main object of all the business concerns is to earn profit. Profit is the measurement of the efficiency of the business. Profitability ratios measure the various aspects of the profitability of a company, such as (*i*) What is the rate of profit on sales? (*ii*) Whether the profits are increasing or decreasing, and if decreasing, the cause of their decrease? Some important profitability ratios are :

(*i*) Gross Profit Ratio
(*ii*) Operating Ratio
(*iii*) Net Profit Ratio
(*iv*) Operating Profit Ratio
(*v*) Earning Per Share
(*vi*) Price Earning Ratio
(*vii*) Return on Investment

(A) Liquidity Ratios (Short-term Solvency Ratios)

(*i*) **Current Ratio or Working Capital Ratio** :– This ratio explains the relationship between current assets and current liabilities of a business. The formula for calculating the ratio is :—

$$\boxed{\text{Current Ratio} = \frac{\text{Current Assets}}{\text{Current Liabilities}}}$$

Current Assets : Current assets are the assets which are likely to be converted into cash or cash equivalents within 12 months from the date of Balance Sheet or within the period of operating cycle.

Current Assets include the following assets :

- Current Investments,
- Inventories (Excluding Loose Tools, Stores and Spares),
- Trade Receivables (Bills Receivables and Sundry Debtors *less* provision for doubtful debts).
- Cash and Bank Balance (Cash in hand, Cash at bank, Cheques/drafts in hand etc.),
- Short term Loans and Advances, and
- Other Current Assets (restricted to prepaid expenses, accrued incomes and advance tax).

Items Excluded from Current Assets :

(*i*) Loose Tools, Stores and Spares
(*ii*) Provision for Doubtful Debts

Current Liabilities : Current liabilities are the liabilities payable within 12 months from the date of Balance Sheet or within the period of Operating Cycle.

Current liabilities include the following liabilities :

- Short term Borrowings (including Bank Overdraft),
- Trade Payables (Bills Payables and Sundry Creditors),
- Other Current Liabilities (Current maturities of long term debts, interest accrued on borrowings, income received in advance, outstanding expenses, unclaimed dividends, calls in advance etc.),
- Short term Provisions (Provision for Tax).

Objectives and Significance :—This ratio is used to assess the firm's ability to meet its short-term liabilities on time. According to accounting principles, a current ratio of 2 : 1 is supposed to be an ideal ratio. It means that current assets of a business should, at least, be twice of its current liabilities. The higher the ratio, the better it is, because the firm will be able to pay its current liabilities more easily. The reason of assuming 2 : 1 as the ideal ratio is that the current assets include such assets as inventory, trade receivables etc., from which full amount cannot be realised in case of need. Hence, even if half the amount is realised from the current assets on time, the firm can still meet its current liabilities in full.

If the current ratio is less than 2 : 1, it indicates lack of liquidity and shortage of working capital. But a much higher ratio, even though it is beneficial to the short-term creditors, is not necessarily good for the company. A much higher ratio than 2 : 1 may indicate the poor investment policies of the management.

A much higher ratio may be considered to be adverse from the view point of management on account of the following reasons :

(I) A much higher ratio indicates that inventory might be piling up because of poor sales.

(II) Large amount is locked up in trade receivables due to inefficient collection policy.

(III) The cash or bank balances might be lying idle because of no proper investment opportunities are available.

The biggest drawback of the current ratio is that it is susceptible to "window-dressing". This ratio can be improved by an equal decrease in both current assets and current liabilities. For example, if the current assets of a company are ₹2,25,000 and current liabilities are ₹1,25,000, its current ratio in this case will be $\frac{2,25,000}{1,25,000} = 1.8 : 1$. If this company pays off its trade payables by ₹25,000, the current ratio will be : $\frac{2,00,000}{1,00,000} = 2 : 1$.

It is, therefore, dangerous to use this ratio alone as an index of measuring the short-term financial position of a concern.

Following points should be carefully considered while calculating the current ratio:—

(1) Only those assets, which are expected to be realised within a year, should be included in current assets.

(2) Only those liabilities, which are expected to be paid within a year, should be included in current liabilities. Those long-term loans and debentures, which will be due for payment within one year, are also included in current liabilities.

(3) The term 'investment' is used for 'Non Current Investments'. Trade Investments are also treated as 'Non Current Investments'. But 'Current Investments', 'Short-term Investments' and 'Marketable securities' should be included in current assets.

(4) Loose Tools, Patents, Goodwill, Trade Marks and Computer Software are not included in current assets.

(5) 'Bank Overdraft' should be included in current liabilities.

(6) 'Loan', 'Loan on Mortgage' and 'Bank Loan' are long-term borrowings, therefore, these should not be included in current liabilities.

ILLUSTRATION 1.

From the following, compute the Current Ratio and give your comments on it :

	₹
Non-Current Investments	1,00,000
Current Investments	40,000
Inventories (including Loose Tools of ₹50,000)	2,80,000
Trade Receivables :	
Sundry Debtors	1,60,000
Bills Receivables	20,000
Trade Payables :	
Sundry Creditors	1,20,000
Bills Payables	10,000
Long-term Borrowings	2,00,000
Short-term Borrowings	50,000
Short-term Provision (Provision for Tax)	20,000
Cash and Bank Balance	30,000

SOLUTION :

$$\text{Current Ratio} = \frac{\text{Current Assets}}{\text{Current Liabilities}}$$

Current Assets = Current Investments + Inventories (Excluding Loose Tools) + Trade Receivables (Sundry Debtors + Bills Receivables) + Cash and Bank Balance

= ₹40,000 + ₹2,30,000 + ₹1,60,000 + ₹20,000 + ₹30,000

= ₹4,80,000

Current Liabilities = Trade Payables (Sundry Creditors + Bills Payables) + Short term Borrowings + Short term Provision (Provision for Tax)

= ₹1,20,000 + ₹10,000 + ₹50,000 + ₹20,000

= ₹2,00,000

$$\text{Current Ratio} = \frac{₹4{,}80{,}000}{₹2{,}00{,}000} = 2.4 : 1.$$

Comments :— An ideal current ratio should be 2 : 1, which denotes that the current assets of a business should atleast be twice of its current liabilities. Current ratio of this company is 2.4 : 1. Therefore, it can be said that the short-term financial position of the company is satisfactory. This company is in a position to pay its current liabilities in time.

(ii) **Quick Ratio or Acid Test Ratio or Liquid Ratio** :—Quick ratio indicates whether the firm is in a position to pay its current liabilities within a month or immediately. As such, the quick ratio is calculated by dividing liquid assets (Quick Assets) by current liabilities :—

$$\text{Quick Ratio or Acid Test Ratio} = \frac{\text{Quick Assets}}{\text{Current Liabilities}}$$

OR

$$\frac{\text{All Current Assets} - \text{Inventories} - \text{Prepaid Expenses}}{\text{Current Liabilities}}$$

OR

$$\frac{\text{Liquid Assets}}{\text{Current Liabilities}}$$

'Liquid assets' means those assets which will be converted into cash and cash equivalents very shortly. All current assets except inventories and prepaid expenses are included in liquid assets. Inventory is excluded from liquid assets because it has to be sold before it can be converted into cash. Prepaid expenses too are excluded from the list of liquid assets because they are not expected to be converted into cash.

Thus Liquid Assets include the following :

- Current Investments
- Trade Receivables (Bills Receivables and Sundry Debtors *less* Provision for Doubtful Debts)
- Cash and Bank Balance
- Short term Loans and Advances

Or

Liquid Assets = Current Assets – Inventories – Prepaid Expenses and Advance tax.

Objectives and Significance : An ideal quick ratio is said to be 1 : 1. If it is more, it is considered to be better. The idea is that for every rupee of current liabilities, there should atleast be one rupee of liquid assets. This ratio is a better test of short-term financial position of the company than the current ratio, as it considers only those assets which can be easily and readily converted into cash. Inventory is not included in liquid assets as it may take a lot of time before it is converted into cash.

Quick ratio thus is a more rigorous test of liquidity than the current ratio and, when used together with current ratio, it gives a better picture of the short-term financial position of the firm.

Difference between Current Ratio and Quick Ratio

Basis of Distinction	*Current Ratio*	*Quick Ratio (or Liquid Ratio)*
1. Relationship	It establishes a relationship between Current Assets and Current Liabilities.	It establishes a relationship between Liquid Assets and Current Liabilities.
2. Formula for Computation	Current Ratio = $\frac{\text{Current Assets}}{\text{Current Liabilities}}$	Quick Ratio = $\frac{\text{Liquid Assets}}{\text{Current Liabilities}}$
3. Objective	It measures the ability of the firm to meet its current liabilities within 12 months from the date of Balance Sheet or within the period of operating cycle.	It measures the ability of the firm to meet its current liabilities immediately or within a month.

4.	Ideal Ratio	Current Ratio of 2 : 1 is considered as an ideal ratio.	Quick Ratio of 1 : 1 is considered as an ideal ratio.
5.	True Measurement	It is not a true measurement of short-term financial position of the firm as it may include a large amount of inventories which may not be quickly convertible into cash.	It removes this shortcoming of current ratio by excluding the amount of inventories.

ILLUSTRATION 2.

Following particulars are given to you :

		₹
Trade Investments		2,50,000
Marketable Securities		40,000
Tangible Fixed Assets		6,00,000
Intangible Assets (Goodwill)		1,00,000
Trade Receivables	2,00,000	
Less : Provision for Doubtful Debts	20,000	1,80,000
Cash and Bank Balance		80,000
Trade Payables		1,20,000
Rent Payable		10,000
Dividend Payable		30,000
Inventories		3,90,000
Long term Borrowings (8% Debentures)		2,80,000
Short term Borrowings (Bank Overdraft)		25,000
Short term Provisions :		
Provision for Tax		55,000
Income Tax Paid in Advance		30,000

Calculate the Liquidity Ratios and Comment upon the short-term financial position of the company.

SOLUTION :

Liquidity Ratios include the following two ratios :

(*a*) Current Ratio, and (*b*) Quick Ratio

(*a*) Current Ratio $= \dfrac{\text{Current Assets}}{\text{Current Liabilities}}$

Current Assets = Marketable Securities + Trade Receivables* + Cash & Bank Balance + Inventories + Income Tax Paid in Advance

= ₹40,000 + ₹1,80,000 + ₹80,000 + ₹3,90,000 + ₹30,000

= ₹7,20,000

Current Liabilities = Trade Payables + Rent Payable + Dividend Payable + Bank Overdraft + Provision for Tax

= ₹1,20,000 + ₹10,000 + ₹30,000 + ₹25,000 + ₹55,000

= ₹2,40,000

Current Ratio $= \dfrac{₹7{,}20{,}000}{₹2{,}40{,}000} = 3 : 1$

$$(b)\ \text{Quick Ratio} = \frac{\text{Liquid Assets or Quick Assets}}{\text{Current Liabilities}}$$

$$\text{Liquid Assets} = \text{Current Assets} - \text{Inventories} - \text{Income Tax Paid in Advance}$$

$$= ₹7{,}20{,}000 - ₹3{,}90{,}000 - ₹30{,}000$$

$$= ₹3{,}00{,}000$$

$$\text{Current Liabilities} = ₹2{,}40{,}000$$

$$\text{Quick Ratio} = \frac{₹3{,}00{,}000}{₹2{,}40{,}000} = 1.25 : 1$$

Comments : The short-term financial position of the company is sound because its current ratio is 3 : 1, which is more than the ideal ratio of 2 : 1. Liquid ratio of the company is 1.4 : 1, which is also more than the ideal ratio of 1 : 1. Therefore, it can be said that the company is in a position to pay its current liabilities instantly.

- It is important to note that Provision for Doubtful Debts is deducted from Trade Receivables for calculating Current Ratio and Quick Ratio.

ILLUSTRATION 3.

From the following compute Current Ratio :

S. No.	Items	Amount	S. No.	Items	Amount
		₹			₹
1.	Total Assets	1,00,000	3.	Non-Current Liabilities	20,000
2.	Shareholder's Funds	60,000	4.	Non-Current Assets	50,000

SOLUTION

$$\text{Current Ratio} = \frac{\text{Current Assets}}{\text{Current Liabilities}}$$

$$\text{Current Assets} = \text{Total Assets} - \text{Non Current Assets}$$

$$= ₹1{,}00{,}000 - ₹50{,}000 = ₹50{,}000$$

Total of Assets side of Balance Sheet will be equal to total of Equity and Liabilities side.

$$\text{Hence, Current Liabilities} = \text{Total Assets} - \text{Shareholder's Funds} - \text{Non Current Liabilities}$$

$$= ₹1{,}00{,}000 - ₹60{,}000 - ₹20{,}000$$

$$= ₹20{,}000$$

$$\text{Current Ratio} = ₹\frac{50{,}000}{20{,}000} = 2.5 : 1$$

ILLUSTRATION 4.

Calculate the Current Ratio from the following information :

	₹
Total Assets	8,00,000
Fixed Assets	5,40,000
Non Current Investments	1,10,000
Shareholder's Funds	6,00,000
Non Current Liabilities	80,000

SOLUTION :

Current Assets = Total Assets – Fixed Assets – Non Current Investment
= ₹8,00,000 – ₹5,40,000 – ₹1,10,000
= ₹1,50,000

Hence, Current Liabilities = Total Assets – Shareholder's Funds – Non Current Liabilities
= ₹8,00,000 – ₹6,00,000 – ₹80,000
= ₹1,20,000

$$\text{Current Ratio} = \frac{\text{Current Assets}}{\text{Current Liabilities}}$$

$$= \frac{1,50,000}{1,20,000} = 1.25 : 1$$

ILLUSTRATION 5.

The Current Ratio of a Company is 2 : 1. State, giving reasons which of the following transactions would (*i*) improve (*ii*) reduce or (*iii*) not alter, the current ratio :

(*a*) Repayment of a Current Liability
(*b*) Purchasing goods on credit
(*c*) Sale of an Office Equipment for ₹4,000 (Book Value ₹5,000)
(*d*) Sale of goods for ₹11,000 (Cost ₹10,000)
(*e*) Redemption of Debentures.

SOLUTION :

Current Ratio as given in the question is 2 : 1. In order to understand the question in a simple manner, it may be assumed that current assets are ₹2,00,000 and current liabilities are ₹1,00,000.

(*a*) Repayment of a Current Liability : Suppose, a current liability amounting to ₹50,000 is repaid, the revised current ratio will be : –

$$\frac{2,00,000 - 50,000 \text{ (Cash)}}{1,00,000 - 50,000 \text{ (Current Liability)}} = \frac{1,50,000}{50,000} = 3 : 1$$

∴ Current Ratio is improved.

(*b*) Purchasing Goods on Credit : Suppose, goods for ₹25,000 is purchased on credit, the revised current ratio will be :

$$\frac{2,00,000 + 25,000 \text{ (Inventory)}}{1,00,000 + 25,000 \text{ (Trade Payables)}} = \frac{2,25,000}{1,25,000} = 1.8 : 1$$

∴ Current Ratio is reduced.

(c) Sale of an Office Equipment for ₹4,000 (Book Value ₹5,000) : Sale of Office Equipment (*e.g.*, Typewriter etc.) results in an increase in Cash Balance by ₹4,000 and this leads to an increase in current assets. There will be no other effect of the sale of office equipment since it is a fixed asset. As such,

$$\frac{2{,}00{,}000 + 4{,}000 \text{ (Cash)}}{1{,}00{,}000} = \frac{2{,}04{,}000}{1{,}00{,}000} = 2.04 : 1$$

∴ Current Ratio is improved.

(d) Sale of Goods for ₹11,000 (cost ₹10,000) : The revised ratio will be :

$$\frac{2{,}00{,}000 + 11{,}000 \text{ (cash)} - 10{,}000 \text{ (Inventory)}}{1{,}00{,}000} = \frac{2{,}01{,}000}{1{,}00{,}000} = 2.01 : 1$$

∴ Current Ratio is improved.

(e) Redemption of Debentures : Debentures redeemable during the current year are included in current liabilities. Suppose, debentures amounting to ₹10,000 are included in current liabilities and they are now paid off. It will reduce the amount of current liabilities on the one hand and on the other hand it will also reduce the current assets, as the cash balance is reduced because of payment of debentures. Thus, the revised ratio will be :—

$$\frac{2{,}00{,}000 - 10{,}000 \text{ (Cash)}}{1{,}00{,}000 - 10{,}000 \text{ (Debentures Redeemed)}} = \frac{1{,}90{,}000}{90{,}000} = 2.11 : 1$$

∴ Current Ratio is improved.

ILLUSTRATION 6.

Assuming that the Current Ratio is 2 : 1, state, giving reasons, which of the following transactions would (*i*) improve, (*ii*) reduce, or (*iii*) not alter, the current ratio :—

(*i*) Cash collected from Trade Receivables or Cash received against B/R on its maturity.
(*ii*) B/R received from Trade Receivables or B/R drawn.
(*iii*) B/R endorsed to Trade Payables.
(*iv*) B/R dishonoured.
(*v*) Sale of Inventories at par for cash.
(*vi*) Sale of Inventories at profit for cash.
(*vii*) Sale of Inventories at loss for cash.
(*viii*) Sale of Inventories at par on credit.
(*ix*) Sale of Inventories at profit on credit.
(*x*) Sale of Inventories at loss on credit.
(*xi*) Purchase of Inventories for cash.
(*xii*) Purchase of Inventories on credit. *(ISC 2015)*
(*xiii*) Sale of a fixed asset on a credit of 2 months.
(*xiv*) Sale of a fixed asset on long-term deferred payment basis.
(*xv*) Sale of a fixed asset against cheque.
(*xvi*) Purchase of a fixed asset for cash.
(*xvii*) Purchase of a fixed asset on a credit of 2 months.
(*xviii*) Purchase of a fixed asset on long-term deferred payment basis.
(*xix*) Cash paid to Trade Payables or cheque issued against a B/P. *(ISC 2015)*
(*xx*) B/P given to Trade Payables.
(*xxi*) Repayment of a non-current liability (*e.g.*, Long term Loans etc.)

(*xxii*) Conversion of a non current liability into equity shares.
(*xxiii*) Issue of new Shares/Debentures for cash.
(*xxiv*) Issue of new Shares/Debentures against purchase of fixed asset.

SOLUTION :

Statement showing the effect of various transactions on Current Ratio :

Tr. No.	*Current Ratio will*	*Reasons*
(*i*)	Not Alter	Neither the current assets nor the current liabilities are affected since there is only a conversion of one current asset into another current asset.
(*ii*)	Not Alter	Neither the current assets nor the current liabilities are affected since here also, there is only a conversion of one current asset (*i.e.*, Trade Receivables) into another current asset (*i.e.*, B/R).
(*iii*)	Improve	Both the current assets and current liabilities are decreased by the same amount.
(*iv*)	Not Alter	Neither the current assets nor the current liabilities are affected since there is only a conversion of one current asset (*i.e.* B/R) into another current asset (*i.e.*, Trade Receivables).
(*v*)	Not Alter	Neither the current assets nor the current liabilities are affected since there is only a conversion of one current asset into another current asset.
(*vi*)	Improve	Current liabilities remain unchanged but current assets are increased by the amount of profit.
(*vii*)	Reduce	Current liabilities remain unchanged but current assets are decreased by the amount of loss.
(*viii*)	Not Alter	The reason being same as given in point No. (*v*) above.
(*ix*)	Improve	The reason being same as given in point No. (*vi*) above.
(*x*)	Reduce	The reason being same as given in point No. (*vii*) above.
(*xi*)	Not Alter	Neither the current assets nor the current liabilities are affected since there is only a conversion of one current asset into another current asset.
(*xii*)	Reduce	Both the current assets and current liabilities are increased by the same amount.
(*xiii*)	Improve	Current liabilities remain unchanged but current assets are increased.
(*xiv*)	Not Alter	Neither the current assets nor the current liabilities are affected since the non-current assets are increased as well as decreased by the same amount.
(*xv*)	Improve	Current liabilities remain unchanged but current assets are increased.
(*xvi*)	Reduce	Current liabilities remain unchanged but current assets are decreased.
(*xvii*)	Reduce	Current assets remain unchanged but current liabilities are increased.
(*xviii*)	Not Alter	Neither the current assets nor the current liabilities are affected since both the non-current assets and non-current liabilities are increased by the same amount.
(*xix*)	Improve	Both the current assets and current liabilities are decreased by the same amount.
(*xx*)	Not Alter	Neither the current assets nor the current liabilities are affected since here also, there is only a conversion of one current liability into another current liability.

(*xxi*)	Reduce	Current liabilities remain unchanged but current assets are decreased.
(*xxii*)	Not Alter	Neither the current assets nor the current liabilities are affected since there is only a conversion of one non-current liability into another non-current liability.
(*xxiii*)	Improve	Current liabilities remain unchanged but current assets are increased by the amount of cash received on issue of shares or debentures.
(*xxiv*)	Not Alter	Neither the current assets nor the current liabilities are affected since both the non-current assets and the non-current liabilities are increased by the same amount.

ILLUSTRATION 7.

Current Ratio of *X* Ltd. is 2.5 : 1. State with reason, which of the following transactions would (*i*) increase, (*ii*) decrease or (*iii*) not change the ratio :

(*i*) Included in trade payables was a bills payable which was met on maturity.

(*ii*) Trade receivables include debtors of ₹40,000 which were received.

(*iii*) Company purchased furniture of ₹45,000. The Vendor was paid by issue o equity shares of ₹10 each at par.

(*iv*) Redemption of Debentures.

(*v*) Purchase of goods for ₹20,000 against cheque.

(*vi*) Purchase of Loose Tools for ₹10,000 against cheque.

(*vii*) Bills Receivable of ₹2,000 endorsed to a Creditor is dishonoured.

(ISC 2017

(*viii*) ₹8,000 cash collected from Debtors of ₹8,500 in full and final settlement.

(ISC 2017

SOLUTION :

Transaction	*Effect on Current Ratio*	*Reasons*
(*i*)	Increase	Both the Current assets and Current Liabilities have decreased by equal amount.
(*ii*)	No Change	One Current asset (B R) is replaced by another Current asset (Cash o bank).
(*iii*)	No Change	Neither Current assets nor Current liabilities are affected.
(*iv*)	Increase	Both Current assets and Current liabilities have decreased by the sam amount (Debentures redeemable during the current year are treated a Current Liability)
(*v*)	No Change	One Current asset (goods) is replaced by another Current asset (bank
(*vi*)	Decrease	Current assets (bank) will reduce while Loose Tools are not include in Current assets at the time of computing current ratio.
(*vii*)	Decrease	Trade receivables (Debtors) and trade payables (Creditors) wi increase by the same amount.
(*viii*)	Decrease	Current assets will be reduced by ₹500

ILLUSTRATION 8.

State giving reason, whether the Current Ratio will improve or decline or will ha no effect in each one of the following transactions if Current Ratio is (I) 2 : (II) 1 : 1, (III) 0.8 : 1.

(1) Repayment of a Current Liability.
(2) Purchase of goods for cash.
(3) Purchase of goods on credit.
(4) Sale of goods for ₹2,00,000 (Cost ₹1,50,000).
(5) Sale of goods for ₹2,00,000 (Cost ₹2,20,000)
(6) Sale of furniture for ₹40,000 (Book Value ₹50,000).
(7) Bill Receivable endorsed to a Creditor.
(8) Bill Receivable endorsed to a Creditor dishonoured.
(9) Payment of dividend payable.
(10) Bills Payable accepted for one month.

SOLUTION :

Effect on Current Ratio :

S. No.	*If Current Ratio is 2 : 1*	*If Current Ratio is 1 : 1*	*If Current Ratio is 0.8 : 1*	*Reason*
(1)	Improve	No effect	Decline	Both the Current Assets and Current Liabilities will decrease by the same amount.
(2)	No effect	No effect	No effect	One Current Asset (Cash or Bank) is converted into another Current Asset (goods).
(3)	Decline	No effect	Improve	Both the Current Assets and Current Liabilities will increase by the same amount.
(4)	Improve	Improve	Improve	Current Assets are increased by ₹50,000 (Profit) but Current Liabilities remain unchanged.
(5)	Decline	Decline	Decline	Current Assets are decreased by ₹20,000 (Loss) but Current Liabilities remain unchanged.
(6)	Improve	Improve	Improve	Current Assets are increased by ₹40,000 (Cash or Bank) but Current Liabilities remain unchanged.
(7)	Improve	No effect	Decline	Both the Current Assets and Current Liabilities will decrease by the same amount.
(8)	Decline	No effect	Improve	Both the Current Assets and Current Liabilities will increase by the same amount.
(9)	Improve	No effect	Decline	Both the Current Assets and Current Liabilities will decrease by the same amount.
(10)	No effect	No effect	No effect	One Current Liability (Creditor) is converted into another Current Liability (B/P)

ILLUSTRATION 9.

State giving reasons which of the following transactions would Improve; Reduce; or Not change the Quick Ratio if Quick Ratio is (*i*) 1.4 : 1; (*ii*) 1 : 1 or (*iii*) 0.75 : 1.

(*i*) Cash collected from Trade Receivables.
(*ii*) Cash paid to Trade Payables.
(*iii*) Purchase of goods for Cash.

(*iv*) Purchase of goods on Credit of 2 months.
(*v*) Sale of goods costing ₹20,000 for ₹15,000.
(*vi*) Sale of an Office furniture (book value ₹25,000) for ₹5,000.
(*vii*) B/R drawn on trade receivables for 3 months.
(*viii*) B/R endorsed in favour of a Trade Payable.
(*ix*) B/R dishonoured at maturity.
(*x*) B/R collected at maturity.
(*xi*) B/P accepted for 2 months.
(*xii*) B/P paid at maturity.
(*xiii*) Payment of outstanding liabilities.
(*xiv*) Share issue expenses written off.

SOLUTION :

Statement showing the effect of various transactions on Quick Ratio :

Tr. No.	*If Quick Ratio is 1.4 : 1*	*If Quick Ratio is 1 : 1*	*If Quick Ratio is 0.75 : 1*	*Reasons*
(*i*)	Not Change	Not Change	Not Change	Neither the liquid assets nor the current liabilities are affected since there is only a conversion of one liquid asset into another liquid asset.
(*ii*)	Improve	Not Change	Reduce	Both the liquid assets and current liabilities are decreased by the same amount.
(*iii*)	Reduce	Reduce	Reduce	Current liabilities remain unchanged but liquid assets are decreased by outflow of cash.
(*iv*)	Reduce	Reduce	Reduce	Liquid assets remain unchanged but current liabilities are increased.
(*v*)	Improve	Improve	Improve	Current liabilities remain unchanged but liquid assets are increased.
(*vi*)	Improve	Improve	Improve	The reason being same as given in point (*v*) above.
(*vii*)	Not Change	Not Change	Not Change	The reason being same as given in point (*i*) above.
(*viii*)	Improve	Not Change	Reduce	The reason being same as given in point (*ii*) above.
(*ix*)	Not Change	Not Change	Not Change	The reason being same as given in point (*i*) above.
(*x*)	Not Change	Not Change	Not Change	The reason being same as given in point (*i*) above.
(*xi*)	Not Change	Not Change	Not Change	Neither the liquid assets nor the Current liabilities are affected since there is only conversion of one current liability into another current liability.
(*xii*)	Improve	Not Change	Reduce	The reason being same as given in point (*ii*) above.

(xiii)	Improve	Not Change	Reduce	The reason being same as given in point *(ii)* above.
(xiv)	Not Change	Not Change	Not Change	Neither the liquid assets nor the current liabilities are affected.

ILLUSTRATION 10.

Calculate Current Ratio from the following :

Working Capital ₹45,000; Total Debt ₹1,00,000 and Long-term Debt ₹70,000.

SOLUTION :

Current Liabilities = Total Debt – Long term Debt
= ₹1,00,000 – ₹70,000 = ₹30,000

Current Assets = Working Capital + Current Liabilities
= ₹45,000 + ₹30,000 = ₹75,000

$$\text{Current Ratio} = \frac{\text{Current Assets}}{\text{Current Liabilities}} = \frac{₹\ 75,000}{₹\ 30,000} = 2.5 : 1$$

ILLUSTRATION 11.

Calculate Current Ratio from the following :

Working Capital ₹6,00,000; Trade Payables ₹1,80,000 and other Current Liabilities ₹20,000.

SOLUTION :

Current Liabilities = Trade Payables + Other Current Liabilities
= ₹1,80,000 + ₹20,000 = ₹2,00,000

Current Assets = Working Capital + Current Liabilities
= ₹6,00,000 + ₹2,00,000 = ₹8,00,000

$$\text{Current Ratio} = \frac{\text{Current Assets}}{\text{Current Liabilities}} = \frac{₹\ 8,00,000}{₹\ 2,00,000} = 4 : 1$$

ILLUSTRATION 12.

From the following data, calculate Current Ratio and Liquid Ratio :

	₹
Liquid Assets	75,000
Inventories (Includes Loose Tools of ₹20,000)	35,000
Prepaid Expenses	10,000
Working Capital	60,000

(C.B.S.E. Sample Paper, 2019)

SOLUTION :

Current Assets = Liquid Assets + Inventories (excluding loose tools) + Prepaid Expenses
= ₹75,000 + ₹15,000 + ₹10,000
= ₹1,00,000

$$\begin{aligned}\text{Current Liabilities} &= \text{Current Assets} - \text{Working Capital}\\ &= ₹1{,}00{,}000 - ₹60{,}000\\ &= ₹40{,}000\end{aligned}$$

$$\text{Current Ratio} = \frac{\text{Current Assets}}{\text{Current Liabilities}} = \frac{1{,}00{,}000}{40{,}000} = 2.5 : 1$$

$$\text{Liquid Ratio} = \frac{\text{Liquid Assets}}{\text{Current Liabilities}} = \frac{75{,}000}{40{,}000} = 1.875 : 1$$

ILLUSTRATION 13.

Calculate Current Ratio from the following :

Working Capital ₹6,30,000; Current Assets ₹8,40,000 and Inventory ₹4,00,000.

SOLUTION :

$$\text{Current Ratio} = \frac{\text{Current Assets}}{\text{Current Liabilities}}$$

$$\begin{aligned}\text{Current Liabilities} &= \text{Current Assets} \quad \text{Working Capital}\\ &= ₹8{,}40{,}000 - ₹6{,}30{,}000 = ₹2{,}10{,}000\end{aligned}$$

$$\text{Current Ratio} = \frac{₹\ 8{,}40{,}000}{₹\ 2{,}10{,}000} = 4 : 1$$

ILLUSTRATION 14.

A firm had current assets of ₹2,00,000. It then paid a current liability of ₹40,000. After this payment the current ratio was 2 : 1. Determine :—

(*i*) The size of Current Liabilities and Working Capital after the payment.

(*ii*) Also determine the size of these two items before the payment was made.

SOLUTION :

$$\text{Current Ratio} = \frac{\text{Current Assets}}{\text{Current Liabilities}}$$

$$\text{Current Assets} = ₹2{,}00{,}000$$

Current Assets after the payment of ₹ 40,000 : ₹2,00,000 – ₹40,000 = ₹1,60,000.

As current ratio is 2 : 1 and current assets are ₹1,60,000, therefore,

$$\text{Current Liabilities} = \frac{₹\ 1{,}60{,}000}{2} = ₹80{,}000$$

$$\begin{aligned}\text{Working Capital} &= \text{Current Assets} - \text{Current Liabilities}\\ &= ₹1{,}60{,}000 - ₹80{,}000 = ₹80{,}000\end{aligned}$$

Current liabilities before the payment of ₹40,000 must be ₹80,000 + ₹40,000 = ₹1,20,000. Working capital before the payment of ₹40,000 must be ₹2,00,000 – ₹1,20,000 = ₹80,000.

ILLUSTRATION 15.

(*a*) Current Liabilities of a Company are ₹3,50,000. Its current ratio is 3 : 1 and acid test ratio is 1.75 : 1. Calculate the value of Current assets, Liquid assets and Inventories.

(*b*) Current Assets of a Company are ₹3,60,000. Its Current ratio is 2.4 : 1 and acid test ratio is 1.3 : 1. Calculate the value of Current liabilities, liquid assets and Inventories.

(*c*) Working Capital of a company is ₹30,000. Its Current ratio is 2.5 : 1. Calculate the value of (*i*) Current assets (*ii*) Current Liabilities (*iii*) Acid test ratio, assuming Inventories of ₹26,000.

SOLUTION :

(*a*) $$\text{Current Ratio} = \frac{\text{Current Assets}}{\text{Current Liabilities}}$$

$$3 \text{ (Given)} = \frac{\text{Current Assets}}{\text{₹ } 3{,}50{,}000 \text{ (Given)}}$$

$$\therefore \text{ Current Assets} = \text{₹}3{,}50{,}000 \times 3 = \text{₹}10{,}50{,}000$$

$$\text{Acid Test Ratio} = \frac{\text{Liquid Assets}}{\text{Current Liabilities}}$$

$$1.75 \text{ (Given)} = \frac{\text{Liquid Assets}}{\text{₹ } 3{,}50{,}000 \text{ (Given)}}$$

$$\therefore \text{ Liquid Assets} = \text{₹}3{,}50{,}000 \times 1.75 = \text{₹}6{,}12{,}500$$

$$\text{Inventories} = \text{Current Assets} - \text{Liquid Assets}$$

$$= \text{₹}10{,}50{,}000 - \text{₹}6{,}12{,}500 = \text{₹}4{,}37{,}500$$

(*b*) $$\text{Current Ratio} = \frac{\text{Current Assets}}{\text{Current Liabilities}}$$

$$2.4 \text{ (Given)} = \frac{\text{₹ } 3{,}60{,}000 \text{ (Given)}}{\text{Current Liabilities}}$$

$$\therefore \text{ Current Liabilities} = \frac{\text{₹ } 3{,}60{,}000}{2.4} = 3{,}60{,}000 \times \frac{10}{24} = \text{₹}1{,}50{,}000$$

$$\text{Acid Test Ratio} = \frac{\text{Liquid Assets}}{\text{Current Liabilities}}$$

$$1.3 \text{ (Given)} = \frac{\text{Liquid Assets}}{\text{₹ } 1{,}50{,}000 \text{ (Calculated as above)}}$$

$$\therefore \text{ Liquid Assets} = \text{₹}1{,}50{,}000 \times 1.3 = \text{₹}1{,}95{,}000$$

$$\text{Inventories} = \text{Current Assets} - \text{Liquid Assets}$$

$$= \text{₹}3{,}60{,}000 - \text{₹}1{,}95{,}000 = \text{₹}1{,}65{,}000$$

(*c*) (*i*) Working Capital = Current Assets – Current Liabilities

Current Ratio of the company is 2.5 : 1, therefore, based on current ratio the working capital is 2.5 – 1 = 1.5.

If Working Capital is 1.5, Current Assets $= 2.5$

If Working Capital is 1, Current Assets $= \frac{2.5}{1.5}$

If Working Capital is 30,000, Current Assets $= \frac{2.5}{1.5} \times 30{,}000 = \text{₹}50{,}000$

(*ii*) Current Liabilities = Current Assets – Working Capital

= 50,000 – 30,000 = ₹20,000

(*iii*) Acid Test Ratio (Quick Ratio) = $\frac{\text{Liquid Assets}}{\text{Current Liabilities}}$

Liquid Assets = Current Assets – Inventories

= ₹50,000 – ₹26,000 = ₹24,000

Acid Test Ratio = $\frac{24{,}000}{20{,}000}$ = 1.2 : 1.

ILLUSTRATION 16.

A business has a current ratio of 3 : 1 and a quick ratio of 1.2 : 1. If the working capital is ₹1,80,000, calculate the total Current Assets and Inventory.

SOLUTION :

(*i*) Working Capital = Current Assets – Current Liabilities

Current Ratio of the company is 3 : 1, therefore, based on current ratio the working capital is 3 – 1 = 2.

If Working Capital is 2, Current Assets = 3

If Working Capital is 1, Current Assets = $\frac{3}{2}$

If Working Capital is 1,80,000, Current Assets = $\frac{3}{2}$ × 1,80,000 = ₹2,70,000

(*ii*) Current Liabilities = Current Assets – Working Capital

= 2,70,000 – 1,80,000 = ₹90,000

(*iii*) Quick Ratio = $\frac{\text{Liquid Assets}}{\text{Current Liabilities}}$

1.2 (Given) = $\frac{\text{Liquid Assets}}{90{,}000}$

∴ Liquid Assets = ₹90,000 × 1.2 = ₹1,08,000

Inventory = Current Assets – Liquid Assets

= ₹2,70,000 – ₹1,08,000 = ₹1,62,000

ILLUSTRATION 17.

The current assets of Monarch Company are ₹29,745 and the current ratio is 1.5. The inventories stood at ₹8,827. Calculate the liquid ratio and comment on the liquidity position of the company.

SOLUTION :

Current Ratio = $\frac{\text{Current Assets}}{\text{Current Liabilities}}$

1.5 (Given) = $\frac{\text{₹ 29,745 (Given)}}{\text{Current Liabilities}}$

$$\therefore \text{ Current Liabilities} = \frac{₹\ 29{,}745}{1.5} = ₹19{,}830$$

$$\text{Liquid Ratio} = \frac{\text{Liquid Assets}}{\text{Current Liabilities}}$$

$$\text{Liquid Assets} = \text{Current Assets} - \text{Inventories}$$

$$= ₹29{,}745 - ₹8{,}827 = ₹20{,}918$$

$$\text{Liquid Ratio} = \frac{20{,}918}{19{,}830} = 1.05 : 1$$

Comment : The short-term financial position of the enterprise is satisfactory because its liquid ratio is 1.05 : 1, which is a little above than the ideal ratio of 1 : 1.

ILLUSTRATION 18.

Quick Ratio 1.8; Current Assets ₹80,000; Current Liabilities ₹30,000. Calculate the value of Inventory.

SOLUTION :

$$\text{Quick Ratio} = \frac{\text{Liquid Assets}}{\text{Current Liabilities}}$$

$$1.8 \text{ (Given)} = \frac{\text{Liquid Assets}}{₹\ 30{,}000 \text{ (Given)}}$$

$$\therefore \text{ Liquid Assets} = ₹30{,}000 \times 1.8 = ₹54{,}000$$

$$\text{Inventory} = \text{Current Assets} - \text{Liquid Assets}$$

$$= ₹80{,}000 - ₹54{,}000 = ₹26{,}000.$$

ILLUSTRATION 19.

X Ltd's Inventory is ₹1,12,000; Liquid Assets are ₹1,28,000 and quick ratio is 1.6. Work out the current ratio.

SOLUTION :

$$\text{Quick Ratio} = \frac{\text{Liquid Assets}}{\text{Current Liabilities}}$$

$$1.6 \text{ (Given)} = \frac{₹\ 1{,}28{,}000 \text{ (Given)}}{\text{Current Liabilities}}$$

$$\text{Therefore : Current Liabilities} = \frac{₹\ 1{,}28{,}000}{1.6} = ₹80{,}000$$

$$\text{Current Assets} = \text{Liquid Assets} + \text{Inventory}$$

$$= ₹1{,}28{,}000 + ₹1{,}12{,}000 = ₹2{,}40{,}000$$

$$\text{Current Ratio} = \frac{\text{Current Assets}}{\text{Current Liabilities}}$$

$$= \frac{2{,}40{,}000}{80{,}000} = 3 : 1.$$

ILLUSTRATION 20.

A firm has current ratio of 3.5 : 1 and quick ratio of 2 : 1. Assuming inventory at ₹24,000, find out total current assets and total current liabilities.

(C.B.S.E. Sample Paper, 2017)

SOLUTION :

Current Ratio is 3.5 and quick ratio is 2. Difference between current ratio and quick ratio is inventory. Therefore, inventory is 3.5 – 2 = 1.5.

If Inventory is 1.5, Current Assets $= 3.5$

If Inventory is 1, Current Assets $= \frac{3.5}{1.5}$

If Inventory is 24,000, Current Assets $= \frac{3.5}{1.5} \times 24{,}000 = ₹56{,}000$

As Current Ratio is 3.5 : 1 and current assets are ₹56,000

∴ Current Liabilities $= \frac{₹56{,}000}{3.5} = ₹16{,}000.$

ILLUSTRATION 21.

From the following data, calculate Liquid Ratio :—

Current Assets ₹50,000; Inventory ₹13,000; Prepaid Expenses ₹1,000 and Working Capital ₹30,000.

SOLUTION :

Calculation of Liquid Ratio :—

Liquid Assets = Current Assets – Inventory – Prepaid Expenses
= ₹50,000 – ₹13,000 – ₹1,000
= ₹36,000

Current Liabilities = Current Assets – Working Capital
= ₹50,000 – ₹30,000
= ₹20,000

Liquid Ratio $= \frac{\text{Liquid Assets}}{\text{Current Liabilities}} = \frac{₹\ 36{,}000}{₹\ 20{,}000} = 1.8 : 1.$

ILLUSTRATION 22.

The ratio of Current Assets (₹6,00,000) to Current Liabilities (₹4,00,000) is 1.5 : 1. The accountant of the firm is interested in maintaining a Current Ratio of 2 : 1, by paying off a part of the Current Liabilities. Compute the amount of Current Liabilities that should be paid, so that the Current Ratio at the level of 2 : 1 may be maintained.

SOLUTION :

Payment of current liabilities will result in equivalent reduction both in the amount of current assets as well as current liabilities.

Let the amount of current liabilities to be paid $= x$

Thus, Current Ratio $= \dfrac{\text{Current Assets}}{\text{Current Liabilities}} = \dfrac{₹\,6,00,000 - x}{₹\,4,00,000 - x} = 2$

Or $₹8,00,000 - 2x = 6,00,000 - x$

$x = 2,00,000.$

Current liabilities amounting to ₹2,00,000 be paid so that the current ratio may be maintained at the level of 2 : 1.

Verification :

Current Assets after payment of current liabilities of ₹2,00,000

$= 6,00,000 - 2,00,000 = 4,00,000$

Current Liabilities after payment of current liabilities of ₹2,00,000

$= 4,00,000 - 2,00,000 = 2,00,000$

Current ratio after payment $= \dfrac{4,00,000}{2,00,000} = 2 : 1$

ILLUSTRATION 23.

The ratio of Current Assets (₹3,00,000) to Current Liabilities is 2.4 : 1. The accountant of this firm is interested in maintaining a Current Ratio of 2 : 1 by acquiring some Current Assets on Credit. You are required to suggest him the amount of Current Assets which must be acquired for this purpose.

SOLUTION :

Current Ratio $= \dfrac{\text{Current Assets}}{\text{Current Liabilities}}$

2.4 (Given) $= \dfrac{₹\,3,00,000\ (\text{Given})}{\text{Current Liabilities}}$

$\therefore$ Current Liabilities $= \dfrac{₹\,3,00,000}{2.4} = ₹1,25,000$

In order to reduce the Current Ratio, Current Assets must be acquired on credit. But increase in Current Assets on credit results in an increase in Current Liabilities as well. Let's assume the amount of Current Assets to be acquired as x. After the acquisition of Current Assets of ₹x on credit,

Current Assets $= ₹3,00,000 + x$

Current Liabilities $= ₹1,25,000 + x$

Current Ratio $= \dfrac{\text{Current Assets}}{\text{Current Liabilities}}$

2 (Ratio to be maintained) $= \dfrac{₹\,3,00,000 + x}{₹\,1,25,000 + x}$

$₹2,50,000 + 2x = ₹3,00,000 + x$

$\therefore\ x = ₹50,000$

Therefore, Current Assets of ₹50,000 must be acquired on credit to maintain a Current Ratio of 2 : 1.

CASE BASED MCQs — 1

Star Ltd. submits you the following information :

Current Ratio	2.4 : 1
Quick Ratio	1.6 : 1
Working Capital	₹2,80,000

(*a*) Current Liabilities of the company will be

(*i*) ₹4,80,000
(*ii*) ₹2,80,000
(*iii*) ₹ 80,000
(*iv*) ₹2,00,000

(*b*) Inventory of the company will be

(*i*) ₹1,60,000
(*ii*) ₹4,80,000
(*iii*) ₹3,20,000
(*iv*) ₹2,00,000

(*c*) Accountant of the firm wants to maintain current ratio of 2 : 1. Which of the following options will you suggest to him?

(*i*) He may repay current liability of ₹80,000.
(*ii*) He may purchase goods on credit for ₹80,000.
(*iii*) He may sell goods for ₹80,000 on credit.
(*iv*) He may purchase some fixed asset for ₹1,00,000.

(See Answers at the end of the book)

(B) Solvency Ratios

(*i*) **Debt Equity Ratio** : This ratio expresses the relationship between **long-term debts** and **shareholder's funds**. It indicates the proportion of funds which are acquired by long-term borrowings in comparison to shareholder's funds. This ratio is calculated to ascertain the soundness of the long-term financial policies of the firm.

$$\text{Debt Equity Ratio} = \frac{\text{Debt}}{\text{Equity}} \text{ or } \frac{\text{Long term Debts}}{\text{Shareholder's Funds or Net Worth}}$$

Long term Debts :These include 'long term borrowings' and 'Long term Provisions' which mature after one year. For example, Debentures, Mortgage Loan, Bank Loan, Loan from financial institutions and Public Deposits etc.

Shareholder's Funds	include Share Capital and Reserve & Surplus.
Share Capital	include Equity Share Capital and Preference Share Capital
Reserve & Surplus	include Capital Reserve, Securities Premium, General Reserve and Balance in Statement of Profit & Loss.

Objectives and Significance :— This ratio is calculated to assess the ability of the firm to meet its long term liabilities. Generally, debt-equity ratio of 2 : 1 is considered safe. If the debt-equity ratio is more than that, it shows a rather risky financial position from the long-term point of view, as it indicates that more and more funds invested in the business are provided by long-term lenders. A high debt-equity ratio is a danger-signal for long-term lenders.

The lower this ratio, the better it is for long-term lenders because they are more secure in that case. Lower than 2 : 1 debt equity ratio provides sufficient protection to long-term lenders.

ILLUSTRATION 24.

Calculate Debt Equity Ratio from the following particulars :—

	₹
Share Capital	2,50,000
Reserve & Surplus	1,10,000
Long term Borrowings	1,20,000
Long term Provisions	50,000
Current Liabilities	70,000
Non Current Assets	3,80,000
Current Assets	2,20,000

What conclusions do you draw about the company on the basis of this ratio?

SOLUTION :

Debt-Equity Ratio = $\frac{\text{Debt}}{\text{Equity}}$ or $\frac{\text{Long term Debts}}{\text{Shareholder's Funds}}$

Long term Debts = Long term Borrowings + Long term Provisions
₹1,20,000 + ₹50,000 = ₹1,70,000

Calculation of Shareholder's Funds (Equity & Liabilities Side Approach) :

Shareholder's Funds = Share Capital + Reserve & Surplus
₹2,50,000 + ₹1,10,000 = ₹3,60,000

Alternatively, Shareholder's Funds may also be calculated as follows :

Calculation of Shareholder's Funds (Assets Side Approach) :

Shareholder's Funds = Non Current Assets + Working Capital
Non Current Liabilities
Or Non Current Assets + Current Assets – Current Liabilities – Non Current Liabilities i.e. Long term Borrowings and Long Term Provisions
= ₹3,80,000 + ₹2,20,000 – ₹70,000 – ₹1,20,000 – ₹50,000
= ₹3,60,000

Debt Equity Ratio = $\frac{1,70,000}{3,60,000}$ = 0.47 : 1

Conclusion : This ratio indicates the extent of funds provided by long-term lenders in comparison to the funds provided by the owners, *i.e.*, shareholders. The normally acceptable debt-equity ratio is 2 : 1. If this ratio is higher than 2 : 1, it means that long-term borrowings are more than twice in comparison to funds provided by owners and it will indicate a risky financial position. In this question, long-term loans are only 0.47 in comparison to shareholder's funds. It shows that the long-term financial position of the company is sound.

ILLUSTRATION 25.

Calculate Debt Equity Ratio from the following information :

	₹
Equity Share Capital	3,00,000

Preference Share Capital	1,00,000
General Reserve	1,30,000
Securities Premium	40,000
Profit & Loss Balance	70,000
10% Debentures	4,50,000
Loan from Bank	3,50,000
Current Liabilities	20,000

SOLUTION :

Debt Equity Ratio = $\frac{\text{Debt}}{\text{Equity}}$ or $\frac{\text{Long term Debts}}{\text{Shareholder's Funds}}$

Long-term Debts = 10% Debentures + Loan from Bank

= ₹4,50,000 + ₹3,50,000 = ₹8,00,000

Shareholder's Funds = Equity Share Capital + Preference Share Capital + General Reserve + Securities Premium + Profit & Loss Balance

= ₹3,00,000 + ₹1,00,000 + ₹1,30,000 + ₹40,000 + ₹70,000

= ₹6,40,000

Debt Equity Ratio = $\frac{8,00,000}{6,40,000}$ = 1.25 : 1

ILLUSTRATION 26.

Calculate Debt Equity Ratio from the following :

	₹
Land & Building	15,00,000
Plant & Machinery	6,00,000
Intangible Assets	1,00,000
Inventory	5,50,000
Trade Receivables	1,70,000
Trade Payables	1,20,000
Long term Borrowings	12,00,000

SOLUTION :

Debt Equity Ratio = $\frac{\text{Debt}}{\text{Equity}}$ or $\frac{\text{Long term Debts}}{\text{Shareholder's Funds}}$

Long-term Debts = Long term Borrowings

= ₹12,00,000

Shareholder's Funds = Non Current Assets + Working Capital – Non Current Liabilities

Non Current Assets = Land & Building + Plant & Machinery + Intangible Assets

= ₹15,00,000 + ₹6,00,000 + ₹1,00,000 = ₹22,00,000

Working Capital = Current Assets – Current Liabilities

= Inventory + Trade Receivables – Trade Payables

= ₹5,50,000 + ₹1,70,000 – ₹1,20,000 = ₹6,00,000

Non Current Liabilities refer to Long term Debts

Thus, Shareholder's Funds = ₹22,00,000 + ₹6,00,000 – ₹12,00,000

= ₹16,00,000

Debt Equity Ratio = $\frac{₹12,00,000}{₹16,00,000}$ = 0.75 : 1

ILLUSTRATION 27

From the following information, calculate Debt Equity Ratio :

Current Ratio	1.5 : 1
Net Working Capital	₹ 60,000
Inventories	₹ 30,000
Total Assets	₹2,20,000
Total Debt	₹1,60,000

(I.S.C. Specimen Question Paper, 2018)

SOLUTION

Working Capital = Current Assets – Current Liabilities

Current Ratio of the Company is 1.5 : 1, therefore based on Current ratio the Working Capital is 1.5 – 1 = 0.5

If Working Capital is 0.5, Current Liabilities = 1

If Working Capital is 60,000, Current Liabilities = $\frac{1}{0.5}$ × 60,000 = ₹1,20,000

Debt Equity Ratio = $\frac{\text{Debt}}{\text{Equity}}$ or $\frac{\text{Long term Debts}}{\text{Shareholder's Funds}}$

Long Term Debts = Total Debt – Current Liabilities

= 1,60,000 – 1,20,000 = 40,000

Shareholder's Funds = Total Assets – Total Debt

2,20,000 – 1,60,000 = 60,000

Debt Equity Ratio = $\frac{40,000}{60,000}$ = 0.67 : 1

ILLUSTRATION 28

The Debt-Equity Ratio of a Company is 1 : 2. Which of the following would increase, decrease or not change it ?

(*i*) Repayment of Long term Borrowings of ₹40,000.
(*ii*) Purchased a Fixed Asset for ₹50,000 on long-term deferred payment basis.
(*iii*) Issued new equity shares of ₹75,000.
(*iv*) Payment of dividend payable.
(*v*) Goods purchased on Credit.
(*vi*) Issue of Bonus Shares.

SOLUTION :

Debt-Equity Ratio = $\frac{\text{Debt}}{\text{Equity}}$ or $\frac{\text{Long term Debts}}{\text{Shareholder's Funds}}$

In the above question, Debt-Equity Ratio is given as 1 : 2, therefore, it may be assumed that Long-term Debts are ₹1,00,000 and Shareholder's Funds are ₹2,00,000.

(I) By the repayment of Long term Borrowings of ₹40,000, Long-term Debts will be reduced by ₹40,000, and these will stand at ₹1,00,000 – ₹40,000 = ₹60,000. Therefore, the revised ratio will be :—

$$= \frac{₹60{,}000}{₹2{,}00{,}000} = .3 : 1.$$

Before the repayment of Long term Borrowings the ratio was 1 : 2 (or .5 : 1) which is now reduced to .3 : 1. It means that the ratio has decreased.

Therefore, it can be concluded that decrease in long-term debts decreases this ratio.

(II) As a result of credit purchase of a fixed asset for ₹50,000 on long-term payment basis, long-term debts will increase by ₹50,000, and these will stand at ₹1,00,000 + ₹50,000 = ₹1,50,000. Therefore, the revised ratio will be :

$$= \frac{₹1{,}50{,}000}{₹2{,}00{,}000} = .75 : 1$$

Before the purchase of fixed asset, the ratio was 1 : 2 (or .5 : 1) which now stands at .75 : 1. It means that the ratio has increased.

Therefore, it can be concluded that increase in long-term debts increases the ratio.

(III) By the issue of new equity shares, shareholder's funds will be increased and will stand at ₹2,00,000 + ₹75,000 = ₹2,75,000. Therefore, the revised ratio will be :

$$= \frac{₹1{,}00{,}000}{₹2{,}75{,}000} = .36 : 1.$$

Before the issue of equity shares the ratio was 1 : 2 (or .5 : 1) which is now reduced to .36 : 1. It means that the ratio has decreased.

Therefore, it can be concluded that increase in shareholder's funds decreases the ratio.

(IV) Payment of dividend payable means the payment of a current liability. Hence, there will be no change in debt-equity ratio because neither the long-term debts nor the Shareholder's Funds are affected.

(V) Goods purchased on credit will affect only the Inventory and Trade Payables. Hence, there will be no change in debt-equity ratio because neither the long-term debts nor the Shareholder's Funds are affected.

(VI) Issue of bonus shares will not alter the debt equity ratio because neither the long-term debts nor the total equity (Total Shareholder's Funds) is affected.

Note (1) Sometimes, a company issues additional equity shares to the existing equit shareholders in proportion of their existing shareholding in the company without charging an further payment. Such free shares are known as bonus shares. Bonus shares are issued out o reserves and surplus of the company. Hence, because of bonus shares, the reserves and surplu are converted into share capital of the company. Thus total equity (Total shareholder's fund remain unchanged.

Hence, it may be concluded that :—

Decrease in Long-term debts decreases the Debt-Equity Ratio
Increase in Long-term debts increases the Debt-Equity Ratio

Decrease in Shareholder's Funds increases the Debt-Equity Ratio
Increase in Shareholder's Funds decreases the Debt-Equity Ratio

(*ii*) **Debt to Total assets Ratio :—** This ratio is a variation of the debt-equity ratio and gives the same indication as the debt-equity ratio. In this ratio, long-term debts are expressed in relation to total assets. It is calculated as under :—

$$\text{Debt to Total Assets Ratio} = \frac{\text{Debt}}{\text{Total Assets}} \text{ or } \frac{\text{Long term Debts}}{\text{Total Assets}}$$

This ratio is usually expressed as a pure ratio, *i.e.*, 1 : 1 or 2 : 1.

Debt = Long Term Borrowings + Long Term Provisions
Total Assets = Non-Current Assets (Tangible Assets + Intangible Assets + Non-Current Investments + Long Term Loans & Advances) + Current Assets

Examples of Debts are Debentures, Mortgage Loan, Bank Loan, Loans from financial institutions and Public Deposits etc.

Objective and Significance :— This ratio expresses the relationship between long term debts and total assets. It measures the extent to which long term loans are covered by assets which indicates the margin of safety available to providers of long term debts. A lower debt to total assets ratio implies the use of lower debts in financing the assets which means a larger safety margin for lenders. On the other hand, higher ratio represents risky financial position as it implies the use of higher debts in financing the assets of the business.

ILLUSTRATION 29.

Compute Debt to Total Assets Ratio from the following information :

	₹
Fixed Assets	16,00,000
Non Current Investments	2,00,000
Current Assets	7,60,000
Total Debts	18,50,000
Trade Payables	1,40,000
Outstanding Expenses	25,000
Bank Overdraft	85,000

SOLUTION :

$$\text{Debt to Total Assets Ratio} = \frac{\text{Debt (}i.e.\text{, Long term Debt)}}{\text{Total Assets}}$$

Long Term Debts = Total Debts – Trade Payables – Outstanding Expenses – Bank Overdraft
= ₹18,50,000 – ₹1,40,000 – ₹25,000 – ₹85,000
= ₹16,00,000

Total Assets = Fixed Assets + Non Current Investments + Current Assets
= ₹16,00,000 + ₹2,00,000 + ₹7,60,000 = ₹25,60,000

$$\text{Debt to Total Assets Ratio} = \frac{₹16,00,000}{₹25,60,000} = .625 : 1$$

ILLUSTRATION 30.

Calculate Debt to Total Assets Ratio from the following information :

	₹
Shareholder's Funds	14,00,000
Total Debts	16,00,000
Current Liabilities	4,00,000

SOLUTION :

Debt to Total Assets Ratio = $\dfrac{\text{Debt or Long term Debts}}{\text{Total Assets}}$

Long term Debts = Total Debts – Current Liabilities

= ₹16,00,000 – ₹4,00,000 = ₹12,00,000

Total Assets = Shareholder's Funds + Total Debts

= ₹14,00,000 + ₹16,00,000 = ₹30,00,000

Debt to Total Assets Ratio = $\dfrac{₹12,00,000}{₹30,00,000}$ = .4 : 1

ILLUSTRATION 31.

Calculate Debt to Total Assets Ratio from the following information :

	₹		₹
Long-term Borrowings	18,00,000	Share Capital	10,00,000
Long-term Provisions	2,00,000	Security Premium Reserve	3,00,000
Trade Payables	5,00,000	General Reserve	5,00,000
		Surplus *i.e.*, Balance in Statement of Profit and Loss	(2,00,000)

SOLUTION :

Debt to Total Assets Ratio = $\dfrac{\text{Debt or Long term Debts}}{\text{Total Assets}}$

Long term Debts = Long term Borrowings + Long term Provisions

= ₹18,00,000 + ₹2,00,000 = ₹20,00,000

Total Assets = Shareholder's Funds (*i.e.*, Share Capital + Security Premium Reserve + General Reserve + P & L Balance) + Total Debts (*i.e.*, Long term Borrowings + Long term Provisions + Trade Payables)

= ₹10,00,000 + ₹3,00,000 + ₹5,00,000 – ₹2,00,000 + ₹18,00,000 + ₹2,00,000 + ₹5,00,000

= ₹41,00,000

Debt to Total Assets Ratio = $\dfrac{₹20,00,000}{₹41,00,000}$ = .49 : 1

ILLUSTRATION 32.

Calculate the 'Total Assets to Debt Ratio' from the following information :

	₹
Current Assets	11,00,000

Working Capital	6,50,000
Shareholder's Fund	7,50,000
Total Debt	19,50,000
Reserves and Surplus	2,50,000

(C.B.S.E. 2020, Chennai, Mumbai)

SOLUTION :

$$\text{Total Assets to Debt Ratio} = \frac{\text{Total Assets}}{\text{Debt}}$$

Current Liabilities = Current Assets – Working Capital
= ₹11,00,000 – ₹6,50,000 = ₹4,50,000

Debt or Long term Debts = Total Debt – Current Liabilities
= ₹19,50,000 – ₹4,50,000 = ₹15,00,000

Total Assets = Total Debt + Shareholder's Funds
= ₹19,50,000 + ₹7,50,000 = ₹27,00,000

$$\text{Total Assets to Debt Ratio} = \frac{₹27,00,000}{₹15,00,000} = 1.8 : 1$$

Working Note :

Reserve and Surplus will be ignored since it is already included in Shareholder's Funds.

ILLUSTRATION 33.

Calculate Debt to Total Assets Ratio from the following information :

	₹
Capital Employed	40,00,000
Shareholder's Funds	24,00,000
Current Liabilities	4,80,000

SOLUTION :

$$\text{Debt to Total Assets Ratio} = \frac{\text{Debt or Long term Debts}}{\text{Total Assets}}$$

Capital Employed = Shareholder's Funds + Long term Debts
₹40,00,000 = ₹24,00,000 + Long term Debts

Long term Debts = ₹16,00,000

Total Assets = Shareholder's Funds + Long term Debts + Current Liabilities
= ₹24,00,000 + ₹16,00,000 + ₹4,80,000
= ₹44,80,000

$$\text{Debt to Total Assets Ratio} = \frac{₹16,00,000}{₹44,80,000} = .36 : 1$$

(*iii*) **Proprietary Ratio** :— This ratio indicates the proportion of total assets funded by owners or shareholders. It is calculated as under :—

$$\text{Proprietary Ratio} = \frac{\text{Equity}}{\text{Total Assets}}$$

$$\text{or } \frac{\text{Proprietor's Funds or Shareholder's Funds}}{\text{Non Current Assets + Current Assets}}$$

Objectives and Significance : —A higher proprietary ratio is generally treated an indicator of sound financial position from long-term point of view, because it means that a large proportion of total assets is provided by equity and hence the firm is less dependent on external sources of finance. On the contrary, a low proprietary ratio is a danger-signal for Long-term lenders as it indicates a lower margin of safety available to them. The lower the ratio, the less secured are the long-term loans and they face the risk of losing their money.

ILLUSTRATION 34.

Calculate (*i*) Debt-Equity Ratio; (*ii*) Total Assets to Debt Ratio; and (*iii*) Proprietary Ratio from the following particulars :

	₹
Equity Share Capital	3,00,000
Preference Share Capital	1,00,000
General Reserve	1,80,000
Profit & Loss Balance	1,20,000
Debentures	3,00,000
Trade Payables	1,60,000
Outstanding Expenses	40,000

What conclusions do you draw from the above ratios? *(N.C.E.R.T., Modified)*

SOLUTION :

(*i*) Debt Equity Ratio $= \dfrac{\text{Debt}}{\text{Equity}}$ or $\dfrac{\text{Long term Debts}}{\text{Shareholder's Funds}}$

Long term Debts = 8% Debentures

= ₹3,00,000

Shareholder's Funds = Equity Share Capital + Pref. Share Capital + General Reserve + P & L Balance

= 3,00,000 + 1,00,000 + 1,80,000 + 1,20,000

= 7,00,000

Hence, Debt Equity Ratio $= \dfrac{3{,}00{,}000}{7{,}00{,}000} = 0.43 : 1$

Comments : This ratio indicates what proportion of funds are provided by Long-term debts in comparison to Shareholder's funds. Generally, the ratio should not be more than 2 : 1. Debt-Equity ratio of the above company is .43 : 1, which indicates that long-term debts are only .43 in comparison to shareholder's funds. Hence, it may be considered that the long-term financial position of the company is very sound.

(*ii*) Total Assets to Debt Ratio $= \dfrac{\text{Total Assets}}{\text{Debt}}$

Total Assets = Total of Equity and Liabilities side

= Equity Capital + Pref. Capital + General Res. + P & L Bal. + 8% Debentures + Trade Payables + Outstanding Exp.

= ₹3,00,000 + ₹1,00,000 + ₹1,80,000 + ₹1,20,000 + ₹3,00,000 + ₹1,60,000 + ₹40,000

= ₹12,00,000.

Total Assets to Debt Ratio $= \dfrac{12{,}00{,}000}{3{,}00{,}000} = 4 : 1$

Comments : Total assets of this company are 4 times in comparison to long- term debts of the company. The higher ratio indicates the use of lower debts in financing the assets which means higher security to lenders.

(*iii*) Proprietary Ratio $= \dfrac{\text{Equity}}{\text{Total Assets}}$ or $\dfrac{\text{Shareholder's Funds}}{\text{Total Assets}}$

$= \dfrac{7{,}00{,}000}{12{,}00{,}000} = 0.58 : 1$ or 58.33%

Comments : Shareholder's Funds of this Company are 58.33% in comparison to total assets of the company. In other words, 58.33% of the total assets of the company are funded by equity which indicates that the long-term financial position of the company is very sound.

ILLUSTRATION : 35.

From the following compute :

(*a*) Debt to Equity Ratio
(*b*) Debt to Total Assets Ratio
(*c*) Proprietary Ratio

S. No.	*Items*	*Amount*
1.	Long-Term Borrowings	1,00,000
2.	Long-Term Provisions	50,000
3.	Current Liabilities	25,000
4.	Non-Current Assets	1,80,000
5.	Current Assets	45,000

SOLUTION :

(*a*) Debt to Equity Ratio $= \dfrac{\text{Debt}}{\text{Equity}}$ or $\dfrac{\text{Long term Debts}}{\text{Shareholder's Funds}}$

Debt = Long Term Borrowings + Long Term Provisions

= ₹1,00,000 + ₹50,000 = ₹1,50,000

Shareholder's Funds = Non Current Assets + Working Capital – Non Current Liabilities

= Non Current Assets + Current Assets – Current Liabilities – Long Term Borrowings – Long Term Provisions

= ₹1,80,000 + ₹45,000 – ₹25,000 – ₹1,00,000 – ₹50,000

= ₹50,000

$$\therefore \text{Debt-Equity Ratio} = ₹\frac{1,50,000}{50,000} = 3:1$$

(*b*) $$\text{Debt to Total Assets Ratio} = \frac{\text{Debt}}{\text{Total Assets}}$$

Debt = Long Term Borrowings + Long Term Provisions
₹1,00,000 + ₹50,000 = ₹1,50,000

Total Assets = Non Current Assets + Current Assets
= ₹1,80,000 + ₹45,000 = ₹2,25,000

$$\therefore \text{Debt to Total Assets Ratio} = ₹\frac{1,50,000}{2,25,000} = .67:1$$

(*c*) $$\text{Proprietary Ratio} = \frac{\text{Shareholder's Funds}}{\text{Total Assets}}$$

Shareholder's Funds = ₹50,000

Total Assets = ₹2,25,000

$$\therefore \text{Proprietary Ratio} = ₹\frac{50,000}{2,25,000} = 0.22:1$$

ILLUSTRATION 36.

Calculate proprietary ratio, if Total assets to Debt ratio is 2 : 1. Debt is ₹5,00,00 Equity share capital is 0.5 times of debt. Preference Share capital is 25% of equit share capital. Net profit before tax is ₹10,00,000 and rate of tax is 40%.

(C.B.S.E. Sample Paper, 202

SOLUTION :

$$\text{Proprietary Ratio} = \frac{\text{Proprietor's Fund}}{\text{Total Assets}}$$

Total Assets = Debts × 2
= ₹5,00,000 × 2 = ₹10,00,000

Proprietor's Funds = Equity Share Capital + Preference Share Capital + Surplus
= (5,00,000 × 0.5) + (5,00,000 × 0.5 × 25%) + (10,00,000 – 40% of 10,00,000)
= 2,50,000 + 62,500 + 6,00,000 = ₹9,12,500

$$\text{Proprietary Ratio} = \frac{9,12,500}{10,00,000}$$

= 0.912 : 1

ILLUSTRATION 37.

From the following information, calculate Proprietary Ratio :

	₹
Equity Share Capital	2,00,000
10% Preference Share Capital	4,75,000
Reserves and Surplus	50,000
Creditors	1,10,000
6% Bank Loan	1,00,000
Fixed Assets	7,00,000
Non-Trade Investments	2,35,000
Current Assets	1,00,000

(I.S.C. Specimen Question Paper, 2018)

SOLUTION

$$\text{Proprietary Ratio} = \frac{\text{Shareholder's Funds}}{\text{Total Assets}}$$

$$\begin{aligned}\text{Shareholder's Funds} &= \text{Equity Share Capital} + 10\%\ \text{Pref. Share Capital} + \text{Reserves \& Surplus}\\ &= ₹2{,}00{,}000 + ₹4{,}75{,}000 + ₹50{,}000\\ &= ₹7{,}25{,}000\end{aligned}$$

$$\begin{aligned}\text{Total Assets} &= \text{Fixed Assets} + \text{Non-Trade Investments} + \text{Current Assets}\\ &= ₹7{,}00{,}000 + ₹2{,}35{,}000 + ₹1{,}00{,}000\\ &= ₹10{,}35{,}000\end{aligned}$$

$$\text{Proprietary Ratio} = \frac{7{,}25{,}000}{10{,}35{,}000} = 0.7 : 1$$

ILLUSTRATION 38.

The following information is available from the books of Greg Foods Limited :

	₹
Equity Share Capital	1,00,000
8% Preference Share Capital	40,000
Reserves and Surplus	60,000
Investments	30,000
Current Assets	70,000

Proprietary Ratio is 0.8 : 1

Assuming that there are no fictitious assets, calculate the value of the fixed assets of the company. *(I.S.C. 2013)*

SOLUTION :

$$\text{Proprietary Ratio} = \frac{\text{Shareholder's Funds}}{\text{Total Assets}}$$

$$\text{or} \quad 0.8 = \frac{1{,}00{,}000 + 40{,}000 + 60{,}000}{\text{Total Assets}}$$

$$0.8 = \frac{2{,}00{,}000}{\text{Total Assets}}$$

$$\text{Total Assets} = \frac{2,00,000}{0.8} = ₹2,50,000$$

Fixed Assets = Total Assets – Investments – Current Assets
= ₹2,50,000 – ₹30,000 – ₹70,000
= ₹1,50,000

(*iv*) **Interest Coverage Ratio :** This ratio is also termed as 'Debt Service Ratio'. This ratio is calculated by dividing the 'profit before charging interest and income-tax' by 'fixed interest charges.'

$$\text{Interest Coverage Ratio} = \frac{\text{Profit before charging Interest and Income Tax}}{\text{Fixed Interest Charges}}$$

= ....times

Profit before interest and income-tax is to be taken for the calculation of this ratio because this is the amount of profit out of which interest and income-tax is to be paid out. Fixed interest charges include interest on fixed (long-term) loans or debentures.

Significance : This ratio indicates how many times the interest charges are covered by the profits available to pay interest charges. A long-term lender is interested in finding out whether the business will earn sufficient profits to pay the interest charges regularly. This ratio measures the margin of safety for long-term lenders. The higher the ratio, more secure the lender is in respect of payment of interest regularly. If profit just equals interest, it is an unsafe position for the lender as well as for the company also, as nothing will be left for shareholders.

An interest coverage ratio of 6 to 7 times is considered appropriate. It also indicates the extent to which profits can decline without in any way affecting the firm's ability to meet its fixed interest obligations.

ILLUSTRATION 39.

From the following details obtained from the financial statements of KX Ltd. for the year ended 31st March, 2017, calculate Interest Coverage Ratio :

Net Profit after tax ₹6,00,000

₹40,00,000, 12% Debentures of ₹100 each.

Tax Rate 40%

State its significance also. Will the Interest Coverage Ratio change if during the year 2017-18, the company decides to redeem debentures of ₹5,00,000 and expects to maintain the same rate of Net Profit and assume that the Tax rate will not change.

(C.B.S.E. Sample Question Paper, 2018)

SOLUTION :

$$\text{Interest Coverage Ratio} = \frac{\text{Net Profit before Interest and Tax}}{\text{Fixed Interest Charges}}$$

In the above question net profit after interest and tax is given, whereas profit before interest and tax is required to calculate this ratio.

If profit after tax is 60, the profit before tax must be = 100
If profit after tax is ₹6,00,000, the profit before tax must be

$$= \frac{100}{60} \times 6,00,000 = \qquad ₹10,00,000$$

Add :	Interest @ 12% on Debentures of ₹40,00,000	₹ 4,80,000
	Net Profit before Interest and Tax	₹14,80,000

Interest Coverage Ratio $= \dfrac{₹14{,}80{,}000}{₹4{,}80{,}000} = 3.08$ times.

Note : Net Profit after tax means Net Profit after interest and tax

Significance of Interest Coverage Ratio : It reveals the number of times Interest on Long Term Debts is covered by the profits available. A higher ratio ensures safety of interest on Long Term Debts.

The Interest coverage ratio will improve if the company decides to redeem ₹5,00,000 debentures assuming the same rate of Net Profit and the tax rate will be same.

Comments : Normally acceptable interest-coverage ratio is 6 or 7 times, whereas the actual ratio for this company is 3.08. It means that the profits of this company are 3.08 times in comparison to fixed interest charges. This indicates that the firm will not be able to pay the interest on long-term loans regularly. This ratio also indicates that the long-term solvency position of the company is not satisfactory.

ILLUSTRATION 40.

The following particulars are extracted from the Balance Sheet of Goodwill Enterprises Ltd. as at 31st March, 2020 :

	₹
Equity Share Capital	3,00,000
10% Preference Share Capital	1,20,000
Capital Reserve	60,000
Profit & Loss Balance	1,20,000
12% Debentures	50,000
10% Mortgage Loan	1,50,000
Current Liabilities	2,80,000
Non Current Assets	4,80,000
Current Assets	6,00,000

Showing the full working, calculate the following ratios :

(*i*) Debt Equity Ratio

(*ii*) Proprietary Ratio

(*iii*) Interest Coverage Ratio
Net Profit after interest and tax amounted to ₹63,000
Rate of Income Tax was 50%.

SOLUTION :

(*i*) Debt-Equity Ratio $= \dfrac{\text{Debt}}{\text{Equity}}$ or $\dfrac{\text{Long term Debts}}{\text{Shareholder's Funds}}$

Long Term Debts = Debentures + Mortgage Loan
= ₹50,000 + ₹1,50,000 = ₹2,00,000

Shareholder's Funds = Equity Share Capital + Pref. Share Capital
+ Capital Reserve + P & L Balance

= ₹3,00,000 + ₹1,20,000 + ₹60,000 + ₹1,20,000
= ₹6,00,000

Debt Equity Ratio $= \dfrac{₹2,00,000}{₹6,00,000} = .33 : 1$

(*ii*) Proprietary Ratio $= \dfrac{\text{Equity}}{\text{Total Assets}} = \dfrac{\text{Shareholder's Funds}}{\text{Total Assets}}$

Total Assets = Non Current Assets + Current Assets
= ₹4,80,000 + ₹6,00,000 = ₹10,80,000

Proprietary Ratio $= \dfrac{₹6,00,000}{₹10,80,000} = .5556$ or 55.56 %

(*iii*) Interest Coverage Ratio $= \dfrac{\text{Net Profit before Interest and Tax}}{\text{Fixed Interest Charges}}$

Fixed Interest Charges = 12% Interest on Debentures of ₹50,000
+ 10% Interest on Mortgage Loan of ₹1,50,000
= ₹6,000 + ₹15,000 = ₹21,000

Net Profit before Interest and Tax is Calculated as follows :

Net Profit after Interest and Tax = ₹63,000

Net Profit before Tax $= ₹63,000 \times \dfrac{100}{50} = ₹1,26,000$

Net Profit before Interest and Tax = ₹1,26,000 + Fixed Interest Charges
= ₹1,26,000 + ₹21,000
= ₹1,47,000

Interest Coverage Ratio $= \dfrac{₹1,47,000}{₹21,000} = 7$ times.

CASE BASED MCQs — 2

The particulars of Alpha Ltd. are given below:

Particulars	₹
Equity Share Capital	2,00,000
5% Preference Share Capital	60,00
General Reserve	1,20,00
Fixed Assets	5,05,00
Current Assets	1,20,00
Current Liabilities	40,00
Loan @ 10% Interest	5,00,00
Tax provided during the year	30,00
Profit for the current year after Interest and Tax (available for the shareholders)	90,00

(*a*) The Interest Coverage Ratio of the company will be:

(*i*) 1.8 times
(*ii*) 2.8 times
(*iii*) 3.4 times
(*iv*) 2.4 times

(*b*) The Proprietary Ratio of the company will be:

(*i*) 0.47:1 (*ii*) 0.75:1

(*iii*) 0.61:1 (*iv*) 0.38:1

(I.S.C. Sample Paper 2021)

CASE BASED MCQs — 3

Particulars	₹
Current Assets	3,00,000
Fixed Assets	13,00,000
Long term Borrowings	5,00,000
Long term Provisions	3,00,000
6% Debentures	2,00,000
Trade Payables	2,00,000
Share Capital	4,00,000
Shareholder's Funds	6,00,000

(*a*) Total Assets to Debt Ratio will be :

(*i*) 1.6 : 1 (*ii*) 2 : 1

(*iii*) 1.33 : 1 (*iv*) 2.29 : 1

(*b*) Debt Equity Ratio will be :

(*i*) 0.8 : 1 (*ii*) 1.67 : 1

(*iii*) 1 : 1 (*iv*) 1.33 : 1

(*c*) Assuming Debt Equity Ratio of 2 : 1, which of the following will decrease this ratio :

(*i*) Redemption of Preference Shares.

(*ii*) Conversion of Debentures into shares

(*iii*) Purchase of a fixed asset on long-term deferred basis.

(*iv*) Sale of a fixed asset at a loss.

CASE BASED MCQs — 4

Long-term Borrowings	₹36,00,000
6% Debentures	₹ 6,00,000
Current Liabilities	₹ 9,00,000
Debt-Equity Ratio	1.2
Proprietary Ratio	40%

(*a*) Shareholder's Funds will be :

(*i*) ₹35,00,000 (*ii*) ₹30,00,000

(*iii*) ₹42,50,000 (*iv*) ₹37,50,000

(*b*) Total Assets will be :

(*i*) ₹12,00,000 (*ii*) ₹87,50,000

(*iii*) ₹93,75,000 (*iv*) ₹75,00,000

(See answers at the end of the book)

(C) Activity Ratios or Turnover Ratios

These ratios measure how well the facilities at the disposal of the concern are being utilised. These ratios are known as turnover ratios as they indicate the rapidity with which the resources available to the concern are being used to produce revenue from operations (Sales). In other words, these ratios measure the efficiency and rapidity of the resources of the company, like inventory, fixed assets, working capital, trade receivables etc. These ratios are generally calculated on the basis of revenue from operations or cost of revenue from operations. Some of the important activity ratios are discussed below :—

(*i*) **Inventory Turnover Ratio** :— This ratio indicates the relationship between the cost of revenue from operations during the year and average Inventory kept during that year.

$$\text{Inventory Turnover Ratio} = \frac{\text{Cost of revenue from operations}}{\text{Average Inventory}} = \text{.........} \text{ times}$$

(1) Cost of Revenue from Operations can be calculated by two ways :—

(*i*) Cost of Revenue from Operations = Opening Inventory + Purchases + Carriage + Wages + Other Direct Charges – Closing Inventory

OR

(*ii*) Cost of Revenue from Operations = Net Revenue from Operations – Gross Profit.

(2) Average Inventory can be calculated as follows :—

$$\text{Average Inventory} = \frac{\text{Opening Inventory} + \text{Closing Inventory}}{2}$$

Significance :— This ratio indicates whether inventory has been efficiently use or not. It shows the speed with which the inventory is rotated into Revenue fro Operations or the number of times the inventory is turned into Revenue fro Operations during the year. The higher the ratio, the better it is, since it indicates tha inventory is selling quickly. In a business where inventory turnover ratio is high, good can be sold at a low margin of profit and even then the profitability may be quite hig

A low inventory turnover ratio indicates that inventory does not sell quickly an remains lying in the godown for quite a long time. This results in increased storag costs, blocking of funds and losses on account of goods becoming obsolete unsaleable.

This ratio can be used for comparing the efficiency of sales policies of two firm doing same type of business. The inventory policy of the management of that firm whose inventory turnover ratio is higher, will be treated as more efficient.

Similarly, by comparing the inventory turnover ratio of current year with th previous year, the management can assess whether inventory has been more efficientl used or not.

ILLUSTRATION 41.

Calculate inventory turnover ratio from the data given below :

	₹
Inventory at the beginning of the year	90,000
Inventory at the end of the year	1,10,000
Purchases	2,30,000
Wages	70,000
Carriage inwards	20,000
Revenue from Operations (Sales)	4,00,000

SOLUTION :

$$\text{Inventory Turnover Ratio} = \frac{\text{Cost of Revenue from Operations (Cost of Goods Sold)}}{\text{Average Inventory}}$$

$$\begin{aligned}\text{Cost of Revenue from Operations} &= \text{Opening Inventory} + \text{Purchases} + \text{Wages} \\ &\quad + \text{Carriage Inwards} - \text{Closing Inventory} \\ &= ₹90,000 + ₹2,30,000 + ₹70,000 \\ &\quad + ₹20,000 - ₹1,10,000 \\ &= ₹3,00,000\end{aligned}$$

$$\begin{aligned}\text{Average Inventory} &= \frac{\text{Opening Inventory} + \text{Closing Inventory}}{2} \\ &= \frac{₹90,000 + ₹1,10,000}{2} = ₹1,00,000\end{aligned}$$

$$\text{Inventory Turnover Ratio} = \frac{₹3,00,000}{₹1,00,000} = 3 \text{ times}$$

Average Age of Inventory : Inventory Turnover ratio can also be converted into number of days, in the following manner

$$\text{Average Age of Inventory} = \frac{\text{Days in a year}}{\text{Inventory Turnover Ratio}}$$

Average age of inventory is also termed 'Inventory Holding Period'.

ILLUSTRATION 42.

From the following information related to a company calculate inventory turnover ratio :

	₹
Inventory in the beginning	30,000
Inventory at the end	50,000
Net Purchases	5,00,000
Wages	25,000
Salaries	40,000
Revenue from Operations	8,00,000
Carriage Outwards	4,000
Carriage Inwards	5,000
Returns Outwards	30,000

(C.B.S.E. 2020, Delhi)

SOLUTION :

$$\text{Inventory Turnover Ratio} = \frac{\text{Cost of Revenue from Operations}}{\text{Average Inventory}}$$

$$\begin{aligned}\text{Cost of Revenue from Operations} &= \text{Opening Inventory} + \text{Net Purchases} \\ &\quad (\textit{i.e.}, \text{Purchase} - \text{Returns Outwards}) \\ &\quad + \text{Wages} + \text{Carriage Inwards} \\ &\quad - \text{Closing Inventory} \\ &= ₹30{,}000 + ₹5{,}00{,}000^{(1)} + ₹25{,}000 + ₹5{,}000 \\ &\quad - ₹50{,}000 = ₹5{,}10{,}000\end{aligned}$$

$$\text{Average Inventory} = \frac{\text{Opening Inventory} + \text{Closing Inventory}}{2}$$

$$= \frac{30{,}000 + 50{,}000}{2} = 40{,}000$$

$$\text{Inventory Turnover Ratio} = \frac{5{,}10{,}000}{40{,}000} = 12.75 \text{ times}$$

Notes :

(1) Net Purchases (*i.e.*, Purchase – Returns Outwards) ₹5,00,000 are already given in the question. Hence, Return Outwards will not be deducted from ₹5,00,000.

(2) Salaries and Carriage Outwards will be ignored while calculating Inventory Turnover Ratio because these are indirect expenses.

ILLUSTRATION 43.

From the following Statement of Profit and Loss of Kaveri Ltd., Calculate Inventory Turnover Ratio.

STATEMENT OF PROFIT AND LOSS

for the year ended 31st March, 2020

Particulars	*Note No.*	₹
I. Revenue from Operations (Sales)		8,00,000
II. Other Income		25,000
III. Total Revenue (I + II)		8,25,000
IV. Expenses :		
Purchase of Stock in Trade		5,40,000
Change in Inventories of Stock in Trade	1	20,000
Employee Benefit Expenses		90,000
Depreciation and Amortization Exp.		15,000
Other Exp.		10,000
Total Expenses		6,75,000
V. Profit before Tax (III – IV)		1,50,000
Less : Tax		30,000
VI. Profit after Tax		1,20,000

Notes to Accounts :

Particulars	₹
1. **Change in Inventories of Stock in Trade :**	
Opening Inventory	80,000
Less : Closing Inventory	60,000
	20,000

SOLUTION :

$$\text{Inventory Turnover Ratio} = \frac{\text{Cost of Revenue from Operations}}{\text{Average Inventory}}$$

$$\text{Cost of Revenue from Operations} = \text{Purchase of Stock in Trade} + \text{Change in Inventory of Stock in Trade}$$

$$= \text{₹}5{,}40{,}000 + \text{₹}20{,}000 = \text{₹}5{,}60{,}000$$

$$\text{Average Inventory} = \frac{\text{Operning Inventory} + \text{Closing Inventory}}{2}$$

$$= \frac{\text{₹}80{,}000 + \text{₹}60{,}000}{2} = \text{₹}70{,}000$$

$$\text{Inventory Turnover Ratio} = \frac{\text{₹}5{,}60{,}000}{\text{₹}70{,}000} = 8 \text{ times.}$$

ILLUSTRATION 44.

Calculate (*i*) Inventory Turnover Ratio and (*ii*) Average Age of Inventory from the following :

STATEMENT OF PROFIT & LOSS

for the year ended 31st March, 2020

Particulars	*Note No.*	₹
I. Revenue from Operations (Sales)		5,00,000
II. Expenses		
(*a*) Purchase of Stock in Trade		2,50,000
(*b*) Change in Inventories of Stock in Trade	1	(8,000)
(*c*) Employee Benefit Exp.	2	90,000
(*d*) Other Expenses	3	48,000
Total Expenses		3,80,000
III. Profit before Tax (I – II)		1,20,000

Notes to Accounts :

(1) Change in Inventories of Stock in Trade	
Opening Inventory	60,000
Less : Closing Inventory	68,000
	(8,000)

(2) Employee Benefit Expenses :	
Wages	58,000
Salaries	32,000
	90,000

(3) Other Expenses :	
Carriage Inwards	20,000
Carriage Outwards	15,000
Miscellaneous Expenses	13,000
	48,000

SOLUTION :

(*i*) Inventory Turnover Ratio $= \dfrac{\text{Cost of Revenue from Operations}}{\text{Average Inventory}}$

Cost of Revenue from Operations = Purchase of Stock in Trade + Change in Inventory of Stock in Trade + Employee Benefit Exp. (Wages) + Other Exp. (Carriage Inward)

$= ₹2{,}50{,}000 - ₹8{,}000 + ₹58{,}000 + ₹20{,}000$

$= ₹3{,}20{,}000$

Average Inventory $= \dfrac{60{,}000 + 68{,}000}{2} = ₹64{,}000$

Inventory Turnover Ratio $= \dfrac{3{,}20{,}000}{64{,}000} = 5$ times.

(*ii*) Average Age of Inventory $= \dfrac{\text{Days in a year}}{\text{Inventory Turnover Ratio}}$

$= \dfrac{365}{5} = 73$ days

Inventory age of 73 days implies that, on an average, the money blocked in inventory gets converted into revenue from operations in 73 days. If the inventory turnover ratio goes up, the average age of inventory will go down and vice versa.

ILLUSTRATION 45.

Calculate Inventory-turnover Ratio from the following informations, when gross-profit ratio is 25% :

	₹
Credit Sales	2,70,000
Cash Sales	1,50,000
Return Inward	20,000
Opening Inventory	55,000
Closing Inventory	45,000

SOLUTION :

Inventory Turnover Ratio $= \dfrac{\text{Cost of Revenue from Operations}}{\text{Average Inventory}}$

Revenue from Operations = Credit Sales + Cash Sales – Return Inward

$= ₹2{,}70{,}000 + ₹1{,}50{,}000 - ₹20{,}000$

$= ₹4{,}00{,}000$

Cost of Revenue from Operations = Revenue from Operations – Gross Profit

= ₹4,00,000 – 25% of ₹4,00,000

= ₹4,00,000 – ₹1,00,000 = ₹3,00,000

Average Inventory $= \dfrac{\text{Opening Inventory + Closing Inventory}}{2}$

$= \dfrac{\text{₹}55{,}000 + \text{₹}45{,}000}{2} = \text{₹}50{,}000$

Inventory Turnover Ratio $= \dfrac{\text{₹}3{,}00{,}000}{\text{₹}50{,}000} = 6$ times.

ILLUSTRATION 46.

Opening Inventory ₹29,000; Closing Inventory ₹31,000; Revenue from Operations ₹3,20,000; Gross Profit Ratio 25% on sales. Calculate (*i*) Inventory Turnover Ratio and (*ii*) Average Age of Inventory.

SOLUTION :

(*i*) Cost of Revenue from Operations = Revenue from Operations – Gross Profit

= ₹3,20,000 – 25% of 3,20,000

= ₹3,20,000 – 80,000 = ₹2,40,000

Average Inventory $= \dfrac{\text{₹ }29{,}000 + \text{₹ }31{,}000}{2} = \text{₹}30{,}000$

Inventory Turnover Ratio $= \dfrac{\text{Cost of Revenue from Operations}}{\text{Average Inventory}}$

$= \dfrac{\text{₹}2{,}40{,}000}{\text{₹}30{,}000} = 8$ times.

(*ii*) Average Age of Inventory (or Inventory Holding Period) =

$$\frac{\text{Days in a year}}{\text{Inventory Turnover Ratio}} = \frac{365}{8} = 46 \text{ days}$$

ILLUSTRATION 47.

From the following, calculate Inventory Turnover Ratio :

	₹
Opening Inventory	28,000
Closing Inventory	52,000
Revenue from Operations	6,00,000
Gross Profit	25% on cost of revenue from operations

(ISC Sample Paper 2017)

SOLUTION :

Inventory Turnover Ratio $= \dfrac{\text{Cost of Revenue from Operations}}{\text{Average Inventory}}$

Gross Profit is 25% on cost. Hence, goods costing ₹100 is sold for ₹125.

If Revenue from Operations is ₹125, then cost is ₹100

If Revenue from Operations is ₹6,00,000, then Cost $= \frac{100}{125} \times 6,00,000$

$= ₹4,80,000$

Average Inventory $= \frac{\text{Opening Inventory} + \text{Closing Inventory}}{2}$

$= \frac{₹28,000 + ₹52,000}{2} = ₹40,000$

Inventory Turnover Ratio $= \frac{₹4,80,000}{₹40,000} = 12$ times

ILLUSTRATION 48

From the following information obtained from the books of Kundan Ltd., calculat the inventory turnover ratio for the years 2015-16 and 2016-17 :

	2015-16	*2016-17*
	₹	₹
Inventory on 31st March	7,00,000	17,00,000
Revenue from Operations	50,00,000	75,00,000

(Gross profit is 25% on cost of revenue from operations)

In the year 2015-16, inventory increased by ₹2,00,000. (C.B.S.E. 201

SOLUTION :

Inventory Turnover Ratio $= \frac{\text{Cost of Revenue from Operations}}{\text{Average Inventory}}$

Year 2015-16

Cost of Revenue from Operations $= 50,00,000 \times \frac{100}{125} = 40,00,000$

Average Inventory $= \frac{5,00,000 + 7,00,000}{2} = ₹6,00,000$

Inventory Turnover Ratio $= \frac{40,00,000}{6,00,000} = 6.67$ times.

Year 2016-17

Cost of Revenue from Operations $= 75,00,000 \times \frac{100}{125} = 60,00,000$

Average Inventory $= \frac{7,00,000 + 17,00,000}{2} = ₹12,00,000$

Invenory Turnover Ratio $= \frac{60,00,000}{12,00,000} = 5$ times

ILLUSTRATION 49.

Calculate Inventory Turnover Ratio from the following information :

	₹
Cost of Revenue from Operations	5,40,000
Purchases	5,50,000

Direct Expenses	30,000
Opening Inventory	70,000

SOLUTION :

Cost of Revenue from Operations = Opening Inventory + Purchases + Direct Expenses Closing Inventory

₹5,40,000 = ₹70,000 + ₹5,50,000 + ₹30,000 – Closing Inventory

Closing Inventory = ₹6,50,000 ₹5,40,000

= ₹1,10,000

$$\text{Average Inventory} = \frac{\text{Opening Inventory} + \text{Closing Inventory}}{2}$$

$$= \frac{₹70{,}000 + ₹1{,}10{,}000}{2} = ₹90{,}000$$

$$\text{Inventory Turnover Ratio} = \frac{\text{Cost of Revenue from Operations}}{\text{Average Inventory}}$$

$$= \frac{₹5{,}40{,}000}{₹90{,}000} = 6 \text{ times.}$$

ILLUSTRATION 50.

Calculate Inventory Turnover Ratio from the following information :

Revenue from Operations	:	₹10,00,000
Gross Profit	:	20% of Revenue from Operations
Purchases	:	₹8,40,000
Closing Inventory	:	₹1,80,000

SOLUTION :

Cost of Revenue from Operations = Revenue from Operations – Gross Profit

= ₹10,00,000 – 20% of ₹10,00,000

= ₹10,00,000 – ₹2,00,000 = ₹8,00,000

Cost of Revenue from Operations = Opening Inventory + Purchases – Closing Inventory

₹8,00,000 = Opening Inventory + ₹8,40,000 – ₹1,80,000

₹8,00,000 = Opening Inventory + ₹6,60,000

Opening Inventory = ₹1,40,000

$$\text{Average Inventory} = \frac{\text{Opening Inventory} + \text{Closing Inventory}}{2}$$

$$= \frac{₹1{,}40{,}000 + ₹1{,}80{,}000}{2} = ₹1{,}60{,}000$$

$$\text{Inventory Turnover Ratio} = \frac{\text{Cost of Revenue from Operations}}{\text{Average Inventory}}$$

$$= \frac{₹8{,}00{,}000}{₹1{,}60{,}000} = 5 \text{ times}$$

ILLUSTRATION 51.

From the following information, calculate inventory turnover ratio; Revenue from Operations (Sales) ₹16,00,000; Average Inventory ₹2,20,000; Gross Loss Ratio 5%.

(C.B.S.E. 2016, All India)

SOLUTION :

$$\text{Inventory Turnover Ratio} = \frac{\text{Cost of Revenue from Operations}}{\text{Average Inventory}}$$

$$\text{Cost of Revenue from Operations} \quad \text{Revenue from Operations + Gross loss}$$

$$₹16,00,000 + ₹80,000 = ₹16,80,000$$

$$\text{Inventory Turnover Ratio} = \frac{₹16,80,000}{₹2,20,000} = 7.64 \text{ times}$$

ILLUSTRATION 52.

From the following information, calculate Inventory Turnover Ratio :

	₹
Purchases	6,45,000
Carriage Inwards	20,000
Carriage Outwards	15,000
Revenue from Operations	6,00,000
Opening Inventory	80,000
Gross Loss	10% on Revenue from Operations

SOLUTION :

$$\begin{aligned}
\text{Cost of Revenue from Operations} &= \text{Revenue from Operations + Gross Loss} \\
&= ₹6,00,000 + 10\% \text{ of } ₹6,00,000 \\
&= ₹6,60,000
\end{aligned}$$

$$\begin{aligned}
\text{Cost of Revenue from Operations} &= \text{Opening Inventory + Purchases + Carriage Inwards} \\
&\quad - \text{Closing Inventory}
\end{aligned}$$

$$₹6,60,000 = ₹80,000 + ₹6,45,000 + ₹20,000 - \text{Closing Inventory}$$

$$\begin{aligned}
\text{Closing Inventory} &= ₹7,45,000 - ₹6,60,000 \\
&= ₹85,000
\end{aligned}$$

$$\begin{aligned}
\text{Average Inventory} &= \frac{\text{Opening Inventory + Closing Inventory}}{2} \\
&= \frac{₹80,000 + ₹85,000}{2} = ₹82,500
\end{aligned}$$

$$\begin{aligned}
\text{Inventory Turnover Ratio} &= \frac{\text{Cost of Revenue from Operations}}{\text{Average Inventory}} \\
&= \frac{₹6,60,000}{₹82,500} = 8 \text{ times.}
\end{aligned}$$

Working Note : Carriage Inwards is Direct Expenses whereas Carriage Outwards Indirect Expenses. Hence, only Carriage Inwards will be included in Cost of Revenue fro Operations.

ILLUSTRATION 53.

From the given information calculate the inventory turnover ratio :

Revenue from Operations : ₹2,00,000; GP : 25% on cost; Opening Inventory was 1/3rd of the value of Closing Inventory. Closing Inventory was 30% of Revenue from Operations.

SOLUTION :

Gross Profit is 25% on cost. Therefore goods costing ₹100 is sold for ₹125.

Hence, If Revenue from Operations is ₹125,

Cost of Revenue from Operations = ₹100

If Revenue from Operations are ₹2,00,000,

$$\text{Cost of Revenue from Operations} = \frac{100}{125} \times 2,00,000 = ₹1,60,000$$

Closing Inventory is 30% of Revenue from Operations

$$\therefore \text{Closing Inventory} = \frac{30}{100} \times 2,00,000 = ₹60,000$$

$$\text{Opening Inventory} = \frac{1}{3} \times 60,000 = ₹20,000$$

$$\text{Average Inventory} = \frac{\text{Opening Inventory} + \text{Closing Inventory}}{2}$$

$$= \frac{20,000 + 60,000}{2} = ₹40,000$$

$$\text{Inventory Turnover Ratio} = \frac{\text{Cost of Revenue from Operations}}{\text{Average Inventory}}$$

$$= \frac{1,60,000}{40,000} = 4 \text{ times.}$$

ILLUSTRATION 54.

Calculate Inventory Turnover Ratio from the following particulars :

Cost of Revenue from Operations (Cost of Goods Sold)		₹6,40,000
Gross Profit		20% on Sales
Closing Inventory	:	4 times of Opening Inventory
Opening Inventory	:	10% of Cost of Revenue from Operations.

SOLUTION :

(*i*) Opening Inventory is 10% of Cost of Revenue from Operations. Hence,

$$\text{Opening Inventory} = 6,40,000 \times \frac{10}{100} = ₹64,000.$$

(*ii*) Closing Inventory = ₹64,000 × 4 = ₹2,56,000

$$(iii)\ \text{Average Inventory} = \frac{\text{Opening Inventory} + \text{Closing Inventory}}{2}$$

$$= \frac{64,000 + 2,56,000}{2} = ₹1,60,000$$

$$(iv)\ \text{Inventory Turnover Ratio} = \frac{\text{Cost of Revenue from Operations}}{\text{Average Inventory}}$$

$$= \frac{6,40,000}{1,60,000} = 4 \text{ times.}$$

ILLUSTRATION 55.

From the following information, determine the opening inventory and the closing inventory :

Inventory Turnover Ratio	5 times
Revenue from Operations	₹8,00,000
Gross Profit Ratio	25%

Closing inventory was ₹20,000 more than the opening inventory.

(C.B.S.E. 2020, Rajasthan)

SOLUTION :

Revenue from Operations are ₹8,00,000 and G.P. Ratio is 25%,

Hence Gross Profit = $8,00,000 \times \frac{25}{100}$ = ₹2,00,000

Cost of Revenue from Operations = ₹8,00,000 – ₹2,00,000 = ₹6,00,000

$$\text{Average Inventory} = \frac{\text{Cost of Revenue from Operations}}{\text{Inventory Turnover Ratio}}$$

$$= \frac{₹6,00,000}{5} = ₹1,20,000$$

Opening Inventory = ₹1,20,000 – 1/2 of 20,000 = ₹1,10,000

Closing Inventory = ₹1,20,000 + 1/2 of 20,000 = ₹1,30,000

ILLUSTRATION 56.

Cash Revenue from Operations	₹2,00,000
Credit Revenue from Operations	₹4,00,000
Gross Profit	₹1,00,000
Inventory Turnover Ratio	5 Times

Calculate the value of Opening and Closing Inventory in each of the following alternative cases :

Case I If closing inventory was ₹80,000 in excess of opening inventory.

Case II If closing inventory was 3 times that in the beginning.

Case III If closing inventory was 3 times more than that in the beginning.

Case IV If opening inventory was $\frac{1}{3}$rd of inventory at the end.

SOLUTION :

Cost of Revenue from Operations = Cash Revenue from Operations + Credit Revenue from Operations – Gross Profit

= 2,00,000 + 4,00,000 – 1,00,000 = ₹5,00,000

$$\text{Inventory Turnover Ratio} = \frac{\text{Cost of Revenue from Operations}}{\text{Average Inventory}}$$

$$5 \text{ (Given)} = \frac{₹5,00,000}{\text{Average Inventory}}$$

$$\therefore \text{ Average Inventory} = \frac{₹\,5,00,000}{5} = ₹1,00,000$$

Case I Opening Inventory = $₹1,00,000 - \frac{1}{2}$ of $₹80,000$ = 60,000

Closing Inventory = $₹1,00,000 + \frac{1}{2}$ of $₹80,000$ = 1,40,000

Case II Opening Inventory + Closing Inventory = Average Inventory × 2
= $1,00,000 \times 2 = ₹2,00,000$

Since Closing Inventory was 3 times than that in the beginning, ratio between Opening Inventory and Closing Inventory will be 1 : 3.

∴ Opening Inventory = $₹2,00,000 \times \frac{1}{4} = ₹\ 50,000$

Closing Inventory = $₹2,00,000 \times \frac{3}{4} = ₹1,50,000$

Case III Since Closing Inventory was 3 times **more** than that in the beginning, ratio between Opening Inventory and Closing Inventory will be 1 : 4.

∴ Opening Inventory = $₹2,00,000 \times \frac{1}{5} = ₹\ 40,000$

Closing Inventory = $₹2,00,000 \times \frac{4}{5} = ₹1,60,000$

Case IV Since Opening Inventory was $\frac{1}{3}$rd of Closing Inventory, ratio between Opening Inventory and Closing Inventory will be 1 : 3.

∴ Opening Inventory = $₹2,00,000 \times \frac{1}{4} = ₹\ 50,000$

Closing Inventory = $₹2,00,000 \times \frac{3}{4} = ₹1,50,000$

ILLUSTRATION 57.

The Revenue from operations of a firm is ₹6,00,000. Its inventory turnover ratio is 3 times. If gross profit ratio is 25%, calculate its opening inventory and closing inventory. The opening inventory is 25% of closing inventory.

(C.B.S.E. 2020, Punjab)

SOLUTION :

Cost of Revenue from Operations = Revenue from Operations – Gross Profit
= $₹6,00,000 - 25\%$ of $₹6,00,000$
= $₹6,00,000 - ₹1,50,000 = ₹4,50,000$

Inventory Turnover Ratio = $\frac{\text{Cost of Revenue from Operations}}{\text{Average Inventory}}$

3 (Given) = $\frac{4,50,000}{\text{Average Inventory}}$

∴ Average Inventory = $\frac{₹\ 4,50,000}{3} = ₹1,50,000$

Opening Inventory + Closing Inventory = Average Inventory × 2
= $₹1,50,000 \times 2 = ₹3,00,000$

Since Opening Inventory is 25% of Closing Inventory, ratio between Opening Inventory and Closing Inventory will be 25 : 100

Or 1 : 4

$$\therefore \text{ Opening Inventory} = ₹3,00,000 \times \frac{1}{5} = ₹\ 60,000$$

$$\text{Closing Inventory} = ₹3,00,000 \times \frac{4}{5} = ₹2,40,000$$

ILLUSTRATION 58.

₹2,00,000 is the cost of Revenue from Operations, Inventory turnover 8 times; Inventory at the beginning is 1.5 times more than the Inventory at the end. Calculate the values of Opening and Closing Inventory.

SOLUTION :

$$\text{Inventory Turnover Ratio} = \frac{\text{Cost of Revenue from Operations}}{\text{Average Inventory}}$$

$$8 \text{ (Given)} = \frac{₹\ 2,00,000 \text{ (Given)}}{\text{Average Inventory}}$$

$$\therefore \text{ Average Inventory} = \frac{₹\ 2,00,000}{8} = ₹25,000$$

$$\text{Opening Inventory} + \text{Closing Inventory} = \text{Average Inventory} \times 2$$

$$= 25,000 \times 2 = 50,000$$

Since opening inventory is 1.5 times more than that at the end, ratio between opening inventory and closing inventory will be 2.5 : 1.

$$\therefore \text{ Opening Inventory} = ₹50,000 \times \frac{2.5}{3.5} = ₹35,714$$

$$\text{Closing Inventory} = ₹50,000 \times \frac{1}{3.5} = ₹14,286$$

ILLUSTRATION 59.

From the following particulars, determine the amount of gross profit and Revenue from Operations :—

Average Inventory	₹80,000
Inventory Turnover Ratio	6 times
Selling Price	25% above cost

SOLUTION :

$$\text{Inventory Turnover Ratio} = \frac{\text{Cost of Revenue from Operations}}{\text{Average Inventory}}$$

$$6 = \frac{\text{Cost of Revenue from Operations}}{80,000}$$

$$\text{Cost of Revenue from Operations} = 80,000 \times 6 = ₹4,80,000$$

Selling Price is 25% above cost

$\therefore$ Revenue from Operations $= ₹4,80,000 \times \frac{125}{100} = ₹6,00,000$

Hence, Gross Profit is ₹1,20,000.

ILLUSTRATION 60.

From the following particulars, determine the amount of gross profit and revenue from operations :—

Average Inventory	₹95,000
Inventory Turnover Ratio	3 times
Gross Profit	25% of Revenue from Operations

SOLUTION :

$$\text{Inventory Turnover Ratio} = \frac{\text{Cost of Revenue from Operations}}{\text{Average Inventory}}$$

$$3 \text{ (Given)} = \frac{\text{Cost of Revenue from Operations}}{95,000}$$

$$\text{Cost of Revenue from Operations} = ₹95,000 \times 3 = ₹2,85,000$$

Revenue from operations include a profit of 25% on Revenue from Operations, therefore, goods costing ₹75 must have been sold for ₹100. As such :—

If Cost of Revenue from Operations is 75, Revenue from Operations are 100
If Cost of Revenue from Operations is 2,85,000,

$$\text{Revenue from Operations are } \frac{100}{75} \times 2,85,000 = ₹3,80,000$$

Gross Profit = Revenue from Operations – Cost of Revenue from Operations
= ₹3,80,000 – ₹2,85,000 = ₹95,000.

ILLUSTRATION 61.

A Company had a liquid ratio of 1.5 : 1 and a current ratio of 2 : 1. Its inventory turnover ratio was 6 times. It had total current assets of ₹2,00,000.

Find out revenue from operations if the goods are sold at 25% profit on cost.

(C.B.S.E. 2020, Delhi)

SOLUTION :

Current Ratio is 2 : 1 and Current Assets are ₹2,00,000 therefore, Current Liabilities $= \frac{2,00,000}{2} = ₹1,00,000$.

Liquid Ratio is 1.5 : 1 and Current Liabilities are ₹1,00,000 therefore, Liquid Assets $= 1,00,000 \times 1.5 = ₹1,50,000$

Inventory = Current Assets – Liquid Assets
= ₹2,00,000 – ₹1,50,000 = ₹50,000

Inventory Turnover Ratio is 6 times, and Inventory is ₹50,000, therefore, Cost of Revenue from Operations is : $50,000 \times 6 = ₹3,00,000$.

$$\text{Revenue from Operations} = ₹3,00,000 \times \frac{125}{100} = ₹3,75,000.$$

ILLUSTRATION 62.

Following information is given to you :—

(I) Inventory Turnover Ratio 5 Times
(II) Inventory at the end is ₹5,000 more than the inventory in the beginning.
(III) Revenue from Operations (all credit) ₹2,00,000
(IV) Gross Profit Ratio 1/4 on cost.
(V) Current Liabilities ₹60,000
(VI) Quick Ratio 0.75.

Calculate (*a*) Cost of Revenue from Operations, (*b*) Opening Inventory and Closing Inventory, and (*c*) Quick Assets and Current Assets.

SOLUTION :

Gross Profit is 1/4th of cost. Therefore, goods costing ₹100 is sold for ₹125.

If Revenue from Operations are 125, Cost is 100

If Revenue from Operations are ₹2,00,000, Cost is $\frac{100}{125} \times 2{,}00{,}000 = ₹1{,}60{,}000$

$$\text{Average Inventory} = \frac{\text{Cost of Revenue from Operations}}{\text{Inventory Turnover Ratio}} \quad \frac{₹1{,}60{,}000}{5} = ₹32{,}000$$

Opening Inventory = ₹32,000 – 1/2 of 5,000 = ₹29,500

Closing Inventory = ₹32,000 + 1/2 of 5,000 = ₹34,500

Current Liabilities are ₹60,000 and Quick Ratio is .75, therefore,

Quick Assets = ₹60,000 × .75 = ₹45,000

Current Assets = Quick Assets + Closing Inventory

= ₹45,000 + ₹34,500 = ₹79,500

ILLUSTRATION 63.

Following information is given to you :

		₹
Revenue from Operations		4,40,000
Less : Purchases	2,50,000	
Changes in Inventories (Opening Inventory – Closing Inventory) (40,000 – 20,000)	20,000	
Direct Expenses	30,000	3,00,000
Gross Profit		1,40,000

BALANCE SHEET
as at 31st March, 2020

Particulars	*Note No.*	₹
I. EQUITY AND LIABILITIES :		
Shareholder's Funds :		
(*a*) Share Capital		3,00,000
(*b*) Reserve and Surplus	1	1,00,000

Current Liabilities :		
(a) Trade Payables		1,50,000
(b) Other Current Liabilities	2	50,000
TOTAL		6,00,000
II. ASSETS :		
Non-Current Assets		4,00,000
Current Assets :		
(a) Inventory		20,000
(b) Trade Receivables		1,00,000
(c) Cash & Bank Balance		80,000
		6,00,000

Notes :		₹
(1)	Reserve & Surplus : Profit & Loss Balance	1,00,000
(2)	Other Current Liabilities : Outstanding Salary	50,000

On the basis of the informations given above, calculate any two of the following ratios :

(i) Current Ratio,
(ii) Inventory Turnover Ratio, and
(iii) Proprietary Ratio.

SOLUTION :

(i) Current Ratio = $\dfrac{\text{Current Assets}}{\text{Current Liabilities}}$

Current Assets = Inventory + Trade Receivables + Cash & Bank Balance

= 20,000 + 1,00,000 + 80,000 = ₹2,00,000

Current Liabilities = Trade Payables + Outstanding Salary

= 1,50,000 + 50,000 = ₹2,00,000

Current Ratio = $\dfrac{2{,}00{,}000}{2{,}00{,}000} = 1 : 1$

(ii) Inventory Turnover Ratio = $\dfrac{\text{Cost of Goods Sold}}{\text{Average Inventory}}$

Cost of Revenue from Operations = Revenue from Operations – Gross Profit

= ₹4,40,000 – ₹1,40,000 = ₹3,00,000

Average Inventory = $\dfrac{\text{Opening Inventory + Closing Inventory}}{2}$

= $\dfrac{₹40{,}000 + ₹20{,}000}{2}$ = ₹30,000

Inventory Turnover Ratio = $\dfrac{₹3{,}00{,}000}{₹30{,}000}$ = 10 Times (*iii*) Proprietary Ratio $= \dfrac{\text{Shareholder's Fund}}{\text{Total Assets}}$

Shareholder's Fund = Share Capital + Profit and Loss Balance

= ₹3,00,000 + ₹1,00,000 = ₹4,00,000

Proprietary Ratio $= \dfrac{4,00,000}{6,00,000} \times 100 = 66.67\%$

(*ii*) **Trade Receivables Turnover Ratio** :— This ratio indicates the relationship between credit Revenue from Operations and average trade receivables during the year :

Trade Receivables Turnover Ratio $= \dfrac{\text{Credit Revenue from Operations (Credit Sales)}}{\text{Average Trade Receivables}}$

= .... times

Trade Receivables include Debtors and Bills Receivable.

Average Trade Receivables are calculated by adding the trade receivables at the beginning of a period as well as at the end of the period and by dividing the total by 2. While calculating this ratio, provision for bad and doubtful debts is not deducted from total trade receivables, so that it may not give a false impression that trade receivables are collected quickly.

If the amount of credit revenue from operations is not given in the question, the ratio may be calculated by taking the figure of total revenue from operations.

Significance :— This ratio indicates the speed with which the amount is collected from trade receivables. The higher the ratio, the better it is, since it indicates that amount from trade receivables is being collected more quickly. The more quickly the trade receivables pay, the less the risk from bad debts, and so the lower the expenses of collection and increase in the liquidity of the firm. A lower trade receivables turnover ratio will indicate the inefficient credit sales policy of the management. It means that credit sales have been made to customers who do not deserve much credit. It is difficult to set up a standard for this ratio. It depends upon the policy of the management and the nature of industry. By comparing the trade receivables turnover ratio of the current year with the previous year, it may be assessed whether the sales policy of the management is efficient or not.

ILLUSTRATION 64.

Calculate debtors turnover ratio from the following data :—	₹
Total Revenue from Operations for the year (Total Sales)	2,00,000
Cash Revenue from Operations for the year (Cash Sales)	40,000
Trade Receivables at the beginning of the year	20,000
Trade Receivables at the end of the year	60,000

SOLUTION :

Trade Receivables Turnover Ratio $= \dfrac{\text{Credit Revenue from Operations (Credit Sales)}}{\text{Average Trade Receivables}}$

Credit Revenue from Operations = Total Revenue from Operations – Cash Revenue from Operations

= ₹2,00,000 – ₹40,000 = ₹1,60,000

Average Trade Receivables

$$= \frac{\text{Opening Trade Receivables + Closing Trade Receivables}}{2}$$

$$= \frac{₹\ 20{,}000 + ₹\ 60{,}000}{2} = ₹40{,}000$$

Trade Receivables Turnover Ratio $= \dfrac{1{,}60{,}000}{40{,}000} = 4$ Times.

Average Collection Period : Trade Receivables turnover ratio can also be converted into number of days within which the cash is collected from trade receivables. It is calculated as under :

$$\text{Average Collection Period} = \frac{365}{\text{Trade Receivables Turnover Ratio}} = \text{Number of Days}$$

OR

$$= \frac{12}{\text{Trade Receivables Turnover Ratio}} = \text{Number of Months}$$

ILLUSTRATION 65.

From the following details, calculate Trade Receivables Turnover Ratio and Average Collection Period :—

	₹
Total Revenue from Operations for the year (Total Sales)	2,25,000
Cash Revenue from Operations (Cash Sales) : 20% of Total Revenue from Operations	
Revenue from Operations Returns — Out of Credit Revenue from Operations	20,000
Trade Receivables :	
Opening Balance	8,000
Closing Balance	12,000

SOLUTION :

$$\text{Trade Receivables Turnover Ratio} = \frac{\text{Credit Revenue from Operations (Credit Sales)}}{\text{Average Trade Receivables}}$$

Cash Revenue from Operations = 20% of 2,25,000 = ₹45,000

∴ Credit Revenue from Operations = ₹2,25,000 – ₹45,000 = ₹1,80,000

Credit Revenue from Operations = Credit Revenue from Operations – Revenue from Operations Returns

= ₹1,80,000 – ₹20,000 = ₹1,60,000

Average Trade Receivables

$$= \frac{\text{Opening Trade Receivables + Closing Trade Receivables}}{2}$$

$$= \frac{₹\ 8{,}000 + ₹\ 12{,}000}{2} = ₹10{,}000$$

Trade Receivables Turnover Ratio $= \dfrac{₹\ 1{,}60{,}000}{₹\ 10{,}000} = 16$ times

$$\text{Average Collection Period} = \frac{\text{Days in a year}}{\text{Trade Receivables Turnover Ratio}} = \frac{365}{16} = 23 \text{ days}$$

Average Collection Period of 23 days means that, on an average, trade receivables take 23 days to get converted into cash. In other words, credit sales are locked up in trade receivables for 23 days.

Increase in average collection period indicates the excessive blockage of funds with trade receivables which increases the chances of bad debts. A higher average collection period is thus, an indication of the inefficiency and negligency on the part of management. On the other hand, if there is decrease in average collection period, it indicates prompt payment by trade receivables which reduces the chances of bad debts.

ILLUSTRATION 66.

Calculate Trade Receivables Turnover Ratio and Average Collection Period from the following :

	₹
Total Revenue from Operations for the year (Total Sales)	4,00,000
Cash Revenue from Operations (Cash Sales) : being 25% of Credit Revenue from Operations	
Closing Trade Receivables	1,00,000
Excess of Closing Trade Receivables over Opening Trade Receivables	40,000

SOLUTION :

In order to ascertain the Trade Receivables Turnover Ratio, the figure of Credit Revenue from Operations will have to be ascertained. It is as follows :—

If Credit Revenue from Operations (Credit Sales) are 100,
Cash Revenue from Operations will be 25
Therefore, Total Revenue from Operations will be 100 + 25 = 125
Again, if total Revenue from Operations are 125,
Credit revenue from Operations = 100

If total Revenue from Operations are 4,00,000,

$$\text{Credit Revenue from Operations} = \frac{100}{125} \times 4{,}00{,}000 = ₹3{,}20{,}000$$

Opening Trade Receivables = Closing Trade Receivables – Excess of Closing Trade Receivables over Opening Trade Receivables

$$= ₹1{,}00{,}000 - ₹40{,}000 = ₹60{,}000$$

Average Trade Receivables

$$= \frac{\text{Opening Trade Receivables} + \text{Closing Trade Receivables}}{2}$$

$$= \frac{₹\ 60{,}000 + ₹\ 1{,}00{,}000}{2} = ₹80{,}000$$

$$\text{Trade Receivables Turnover Ratio} = \frac{\text{Credit Revenue from Operations}}{\text{Average Trade Receivables}}$$

$$= \frac{3{,}20{,}000}{80{,}000} = 4 \text{ Times}$$

$$\text{Average Collection Period} = \frac{\text{Days in a year}}{\text{Trade Receivables Turnover Ratio}}$$

$$= \frac{365}{4} = 91.25 \text{ days or } 92 \text{ days}$$

It is to be noted that any fraction of a day such as .25 would, in practice, mean that the payment will be received next day. Hence, in the above case 91.25 days would imply 92 days.

ILLUSTRATION 67.

Calculate debtors turnover ratio and average collection period from the following particulars as on 31st March, 2022 assuming 365 working days in a year :—

	₹		₹
Total Gross Revenue from Operations	11,00,000	Total Debtors on 31-3-2021	55,000
Cash Revenue from Operations	1,65,000	Total Debtors on 31-3-2022	66,000
Revenue from Operations Returns	11,000	Bills Receivable on 31-3-2021	11,000
Provision for Doubtful Debts	1,910	Bills Receivable on 31-3-2022	22,000
		Trade Payables on 31-3-2022	15,000

SOLUTION :

Trade Receivables Turnover Ratio $= \dfrac{\text{Credit Revenue from Operations}}{\text{Average Debtors and B/R}}$

Credit Revenue from Operations $= ₹11,00,000 - ₹1,65,000 - ₹11,000$
$= ₹9,24,000$

Average Debtors and B/R $= \dfrac{55,000 + 66,000 + 11,000 + 22,000}{2} = ₹77,000$

Trade Receivables Turnover Ratio $= \dfrac{9,24,000}{77,000} = 12$ times.

Average Collection Period $= \dfrac{\text{Days in a year}}{\text{Trade Receivables Turnover Ratio}}$

$= \dfrac{365}{12} = 30.42$ days or 31 days

ILLUSTRATION 68.

Calculate Debtors Turnover Ratio from the following information :

	₹
Opening Debtors	1,20,000
Credit Sales	10,00,000
Cash Received from Debtors	9,60,000
Discount Allowed	80,000
Goods returned by Debtors	20,000

SOLUTION :

Debtors Turnover Ratio $= \dfrac{\text{Net Credit Sales}}{\text{Average Debtors}}$

Net Credit Sales $=$ Credit Sales – Sales Returns
$= ₹10,00,000 - ₹20,000 = ₹9,80,000$

$$\text{Average Debtors} = \frac{\text{Opening Debtors} + \text{Closing Debtors}}{2}$$

Figure of Closing Debtors is not given in the question.

$$\text{Closing Debtors} = \text{Opening Debtors} + \text{Credit Sales} - \text{Cash received} - \text{Discount allowed} - \text{Sales Returns}$$

$$= ₹1{,}20{,}000 + ₹10{,}00{,}000 - ₹9{,}60{,}000 - ₹80{,}000 - ₹20{,}000$$

$$= ₹60{,}000$$

$$\text{Average Debtors} = \frac{₹1{,}20{,}000 + ₹60{,}000}{2} = ₹90{,}000$$

$$\text{Debtors Turnover Ratio} = \frac{₹9{,}80{,}000}{₹90{,}000} = 10.89 \text{ times.}$$

ILLUSTRATION 69.

From the following particulars, determine the trade receivables at the end of the year :

Credit Revenue from Operations (Credit Sales)	₹17,52,000
Trade Receivables Turnover Ratio	6 times
Trade Receivables (beginning of the year)	₹ 2,84,000

SOLUTION :

$$\text{Trade Receivables Turnover Ratio} = \frac{\text{Credit Revenue from Operations}}{\text{Average Trade Receivables}}$$

$$6 = \frac{₹17{,}52{,}000}{\text{Average Trade Receivables}}$$

$$\therefore \text{Average Trade Receivables} = \frac{₹17{,}52{,}000}{6} = ₹2{,}92{,}000$$

Calculation of Closing Trade Receivables :

Opening Trade Receivables + Closing Trade Receivables

$$= \text{Average Trade Receivables} \times 2$$

$$= ₹2{,}92{,}000 \times 2 = ₹5{,}84{,}000$$

As Opening Trade Receivables are ₹2,84,000, therefore,

$$\text{Closing Trade Receivables} = ₹5{,}84{,}000 - ₹2{,}84{,}000$$

$$= ₹3{,}00{,}000.$$

ILLUSTRATION 70.

A firm made credit Revenue from Operations (Credit Sales) of ₹5,40,000 during the year. If the trade receivables turnover ratio is 9 times, calculate opening and closing trade receivables, if the closing trade receivables are more by ₹8,000 than the opening trade receivables.

SOLUTION :

$$\text{Trade Receivables Turnover Ratio} = \frac{\text{Credit Revenue from Operations}}{\text{Average Trade Receivables}}$$

$$9 = \frac{\text{₹}5,40,000}{\text{Average Trade Receivables}}$$

$$\therefore \text{ Average Trade Receivables} = \frac{\text{₹}5,40,000}{9} = \text{₹}60,000$$

$$\text{Opening Trade Receivables} = \text{₹}60,000 - 1/2 \text{ of } \text{₹}8,000 = \text{₹}56,000$$

$$\text{Closing Trade Receivables} = \text{₹}60,000 + 1/2 \text{ of } \text{₹}8,000 = \text{₹}64,000$$

ILLUSTRATION 71.

Credit Revenue from Operations (Credit Sales) of *X* Ltd. during the year were ₹3,00,000. If trade receivables turnover ratio is 5 times, calculate trade receivables in the beginning and at the end of the year. You are informed that closing trade receivables are two times in comparison to opening trade receivables.

SOLUTION :

$$\text{Trade Receivables Turnover Ratio} = \frac{\text{Credit Revenue from Operations}}{\text{Average Trade Receivables}}$$

$$5 = \frac{\text{₹}3,00,000}{\text{Average Trade Receivables}}$$

$$\therefore \text{ Average Trade Receivables} = \frac{\text{₹}3,00,000}{5} = \text{₹}60,000$$

Opening trade receivables + Closing trade receivables

$$= \text{Average Trade Receivables} \times 2$$

$$= \text{₹}60,000 \times 2 = \text{₹}1,20,000$$

Ratio between Opening trade receivables and Closing trade receivables is 1 : 2

$$\therefore \text{ Opening trade receivables} = \text{₹}1,20,000 \times \frac{1}{3} = \text{₹}40,000.$$

$$\text{Closing trade receivables} = \text{₹}1,20,000 \times \frac{2}{3} = \text{₹}80,000.$$

ILLUSTRATION 72.

Calculate the amount of Opening Trade Receivables and Closing Trade Receivables from the following figures :

Trade Receivables Turnover Ratio 4 times

Cost of Revenue from Operations (Cost of Goods Sold) ₹6,40,000

Gross Profit Ratio 20%

Closing Trade Receivables were ₹20,000 more than at the beginning.

Cash Revenue from Operations being $33\frac{1}{3}$% of Credit Revenue from Operations.

SOLUTION :

$$\text{Gross Profit} = 20\% \text{ of Revenue from Operations}$$

$$\text{It means if Revenue from Operations (Sales)} = \text{₹}100$$

Gross Profit = ₹20

& Cost of Revenue from Operations = ₹80

If Cost of Revenue from Operations is ₹80, Revenue from Operations is ₹100

If Cost of Revenue from Operations is ₹6,40,000,

Revenue from Operations is $\frac{100}{80} \times$ ₹6,40,000

Total Revenue from Operations = ₹8,00,000

As Cash Revenue from Operations being $33\frac{1}{3}\%$ of Credit Revenue from Operations,

The Ratio of Cash Revenue from Operations and Credit Revenue from Operations = $33\frac{1}{3}\% : 100$ or $1 : 3$ or $\frac{1}{4} : \frac{3}{4}$

Credit Revenue from Operations = ₹8,00,000 $\times \frac{3}{4} =$ ₹6,00,000

Trade Receivables Turnover Ratio = $\frac{\text{Credit Revenue from Operations}}{\text{Average Trade Receivables}}$

4 (Given) = $\frac{₹\ 6,00,000}{\text{Average Trade Receivables}}$

Average Trade Receivables = $\frac{₹\ 6,00,000}{4}$ = ₹1,50,000

Opening Trade Receivables = ₹1,50,000 $- \frac{1}{2}$ of ₹20,000

= ₹1,40,000

Closing Trade Receivables = ₹1,50,000 $+ \frac{1}{2}$ of ₹20,000

= ₹1,60,000

ILLUSTRATION 73.

Calculate the amount of Opening and Closing Trade Receivables from the following :

Trade Receivables Turnover Ratio : 6 Times

Cost of Revenue from Operations ₹6,00,000

Gross Profit Ratio : 20% on cost

Cash Revenue from Operations being 25% of total Revenue from Operations.

Opening Trade Receivables were $\frac{1}{4}$th of Closing Trade Receivables.

SOLUTION :

Gross Profit = $6,00,000 \times \frac{20}{100} =$ ₹1,20,000

Total Revenue from Operations = Cost of Revenue from Operations + Gross Pr

= ₹6,00,000 + 1,20,000 = ₹7,20,000

Credit Revenue from Operations = Total Revenue from Operations – Cash Revenue from Operations

= 7,20,000 – 25% of 7,20,000 = ₹5,40,000

$$\text{Trade Receivables Turnover Ratio} = \frac{\text{Credit Revenue from Operations}}{\text{Average Trade Receivables}}$$

$$\text{Average Trade Receivables} = \frac{₹\,5{,}40{,}000}{6} = ₹90{,}000$$

Total of Opening and Closing Trade Receivables = ₹90,000 × 2 = ₹1,80,000

Since Opening Trade Receivables are $\frac{1}{4}$th of Closing Trade Receivables, ratio between Opening Trade Receivables and Closing Trade Receivables will be 1 : 4

$$\therefore \quad \text{Opening Trade Receivables} = ₹1{,}80{,}000 \times \frac{1}{5} = ₹\ 36{,}000$$

$$\text{Closing Trade Receivables} = ₹1{,}80{,}000 \times \frac{4}{5} = ₹1{,}44{,}000$$

CASE BASED MCQs — 5

Following particulars are related to Fast Cargo Ltd. :

		₹
Trade Payables		1,40,000
Trade Receivables	2,10,000	
Less : Provision for Doubtful Debts	10,000	2,00,000
Inventory (Excluding Loose Tools ₹20,000)		1,49,000
Goodwill		50,000
Cash and Bank balance		36,000
Bank Overdraft		20,000
Marketable Securities		80,000
Outstanding Expenses		10,000
Provision for Tax		30,000
Prepaid Rent		3,000
Cost of Revenue from Operations		6,30,000

Gross profit 25% on Revenue from Operations.

(*a*) Current Ratio of the Company will be :

(*i*) 2.39 times (*ii*) 2.44 times
(*iii*) 2.34 times (*iv*) 2.59 times

(*b*) Quick Ratio of the Company will be :

(*i*) 1.63 times (*ii*) 1.58 times
(*iii*) 1.595 times (*iv*) 1.78 times

(*c*) Trade Receivables Turnover Ratio will be :

(*i*) 4.2 times (*ii*) 4 times
(*iii*) 3.94 times (*iv*) 3.75 times

(See Answers at the end of the book)

ILLUSTRATION 74.

The following figures relate to the years ending 31st December, 2018 and 2019. What do they indicate?

	2018	2019
	₹	₹
Revenue from Operations (Sales)	6,00,000	[illegible]
Revenue from Operations Return (Sales Return)	60,000	[illegible]
Gross Profit on Revenue from Operations	20%	[illegible]
Trade Receivables	59,000	1,06,000
Opening Inventory	1,20,000	
Closing Inventory	1,60,000	2,40,000

In 2018 Trade Receivables increased by ₹10,000. Ascertain the Trade eceivables turnover ratio and the Inventory Turnover Ratio. Give your comments bout the company's performance in 2019.

LUTION

YEAR 2018

Closing trade receivables of 2018 were ₹10,000 more in comparison to the ening trade receivables of 2018. Therefore, the opening trade receivables of 2018 = ,000 – ₹10,000 = ₹49,000.

erefore, Average Trade Receivables

$$= \frac{\text{Opening Trade Receivables} + \text{Closing Trade Receivables}}{2}$$

$$= \frac{49{,}000 + 59{,}000}{2} = ₹54{,}000$$

Trade Receivables Turnover Ratio $= \dfrac{\text{Credit Revenue from Operations}}{\text{Average Trade Receivables}}$

$$= \frac{₹5{,}40{,}000}{54{,}000} = 10 \text{ Times}$$

Inventory Turnover Ratio $= \dfrac{\text{Cost of Revenue from Operations}}{\text{Average Inventory}}$

Cost of Revenue from Operations = ₹5,40,000 *less* 20%

$= ₹5{,}40{,}000 – ₹1{,}08{,}000 = ₹4{,}32{,}000$

Average Inventory $= \dfrac{₹1{,}20{,}000 + ₹1{,}60{,}000}{2} = ₹1{,}40{,}000$

Inventory Turnover Ratio $= \dfrac{4{,}32{,}000}{1{,}40{,}000} = 3.09$ times.

YEAR 2019

Closing trade receivables of 2018 will be treated as the opening trade receivable 2019. Therefore,

Average Trade Receivables $= \dfrac{59{,}000 + 1{,}06{,}000}{2} = 82{,}500$

Trade Receivables Turnover Ratio $= \dfrac{\text{Credit Revenue from Operations}}{\text{Average Trade Receivables}}$

$$= \frac{6{,}60{,}000}{82{,}500} = 8 \text{ times}$$

$$\text{Inventory Turnover Ratio} = \frac{\text{Cost of Revenue from Operations}}{\text{Average Inventory}}$$

$$\text{Cost of Revenue from Operations} = ₹6{,}60{,}000 \textit{ less } 25\%$$

$$= ₹6{,}60{,}000 - ₹1{,}65{,}000 = ₹4{,}95{,}000$$

Closing inventory of 2018 will be treated as the opening inventory of 2019. Therefore,

$$\text{Average Inventory} = \frac{1{,}60{,}000 + 2{,}40{,}000}{2} = ₹2{,}00{,}000$$

$$\therefore \text{Inventory Turnover Ratio} = \frac{4{,}95{,}000}{2{,}00{,}000} = 2.475 \text{ times.}$$

Comments :—(*i*) In 2019 the trade receivables turnover ratio has decreased from 10 times to 8 times. It indicates that amount from trade receivables is not being collected in time.

(*ii*) Inventory turnover ratio has dropped. It shows that the sales policy of the management is not efficient. Unsaleable or obsolete items have been purchased which are included in the inventory of the company.

(*iii*) **Trade Payables Turnover Ratio** : This ratio indicates the relationship between credit purchases and average trade payables during the year :

$$\text{Trade Payables Turnover Ratio} = \frac{\text{Net Credit Purchases}}{\text{Average Trade Payables}} = \text{....... times}$$

Trade Payables include Creditors and Bills Payables

If the amount of credit purchase is not given in the question, the ratio may be calculated on the basis of total purchase.

ILLUSTRATION 75.

Calculate Trade Payables Turnover Ratio from the following information :

	₹
Credit Purchases during the year	6,20,000
Purchase Returns (Out of credit purchase)	20,000
Opening Creditors	1,00,000
Closing Creditors	1,40,000
Opening Bills Payable	25,000
Closing Bills Payable	35,000

SOLUTION :

$$\text{Trade Payables Turnover Ratio} = \frac{\text{Net Credit Purchases}}{\text{Average Creditors} + \text{Average B/P}}$$

$$\text{Net Credit Purchases} = ₹6{,}20{,}000 - ₹20{,}000$$

$$= ₹6{,}00{,}000$$

$$\text{Average Creditors \& B/P} = \frac{₹\,1{,}00{,}000 + ₹\,1{,}40{,}000 + ₹\,25{,}000 + ₹\,35{,}000}{2}$$

$$= ₹1{,}50{,}000$$

$$\text{Trade Payables Turnover Ratio} = \frac{₹\,6{,}00{,}000}{₹\,1{,}50{,}000} = 4 \text{ Times.}$$

Significance : This ratio indicates the speed with which the amount is being paid to trade payables. The higher the ratio, the better it is, since it will indicate that the trade payables are being paid more quickly which increases the credit worthiness of the firm.

Average Payment Period : Trade Payables Turnover Ratio could be converted into Average Payment period which indicates the period which is normally taken by the firm to make payment to its Trade Payables. It is calculated as follows :

$$\text{Average Payment Period} = \frac{\text{365 days}}{\text{Trade Payables Turnover Ratio}}$$

In the above illustration :

$$\text{Average Payment Period} = \frac{365}{\text{4 times}} = \text{91.25 days or 92 days}$$

As stated earlier, any fraction of a day would, in practice, mean that the payment will be made next day. Hence, in the above case 91.25 days would imply 92 days.

(*iv*) **Working Capital Turnover Ratio** :–

$$\text{Working Capital Turnover Ratio} = \frac{\text{Revenue from Operations (Net Sales)}}{\text{Working Capital}} = \text{....... times}$$

$$\text{Working Capital} = \text{Current Assets} - \text{Current Liabilities}$$

Significance :– This ratio is of particular importance in non-manufacturing concerns where current assets play a major role in generating sales. This ratio reveals how efficiently working capital has been utilised in making sales. In other words, it shows the number of times working capital has been rotated in producing sales. A high vorking capital turnover ratio shows efficient use of working capital and quick urnover of current assets like inventory and Trade Receivables. A low working capital urnover ratio indicates under-utilisation of working capital. However, a very high urnover ratio of working capital is also dangerous, as it is a sign of over-trading, *i.e.*, loing business with too little working capital. It is an indicator of the shortage of vorking capital and may put the concern in financial difficulties. On the other hand, a ery low turnover ratio of working capital may be a sign of under-Trading in omparison to working capital, *i.e.*, the working capital is in excess of the requirements f business.

LLUSTRATION 76.

Calculate Working Capital Turnover Ratio from the following information :

	₹
Current Assets	1,80,000
Current Liabilities	30,000
Cost of Revenue from Operations	10,00,000
Gross Profit	20% of Cost

OLUTION :

$$\text{orking Capital Turnover Ratio} = \frac{\text{Revenue from Operations}}{\text{Working Capital}}$$

evenue from Operations = Cost of Revenue from Operations + Gross Profit

= ₹10,00,000 + 20% of ₹10,00,000 = ₹12,00,000

Working Capital = Current Assets – Current Liabilities

= ₹1,80,000 – ₹30,000 = ₹1,50,000.

Working Capital Turnover Ratio $= \frac{₹12,00,000}{₹1,50,000} = 8$ times.

ILLUSTRATION 77.

Calculate Working Capital Turnover Ratio from the following information :

	₹
Current Assets	1,75,000
Current Liabilities	50,000
Cost of Revenue from Operations	10,00,000
Gross Profit	20% of Revenue from Operations
Shareholder's Funds	5,00,000

SOLUTION :

Working Capital Turnover Ratio $= \frac{\text{Revenue from Operations}}{\text{Working Capital}}$

Revenue from Operations = Cost of Revenue from Operations + Gross Profit

Revenue from Operations include a profit of 20% on Revenue from Operations, therefore, goods costing ₹80 must have been sold for ₹100. As such,

If cost of Revenue from Operations is ₹80, Revenue from Operations are ₹100

If cost of Revenue from Operations is ₹10,00,000,

Revenue from Operations are $\frac{100}{80} \times 10,00,000 =$ ₹12,50,000

Working Capital = Current Assets – Current Liabilities

= ₹1,75,000 – ₹50,000

= ₹1,25,000.

Working Capital Turnover Ratio $= \frac{₹12,50,000}{₹1,25,000} = 10$ times.

Note : Shareholder's Funds will be ignored.

ILLUSTRATION 78.

The following figures have been extracted from the records of Allen Cosmetics Limited :

	₹
Cost of revenue from Operations	4,00,000
Current Liabilities	90,000

Profit margin is equal to 20% on revenue from Operations

Working Capital Turnover Ratio is equal to 10 times.

Determine the value of the Current Assets of the company. *(I.S.C. 2013)*

SOLUTION :

Gross Profit = 20% of Revenue from Operations

It means, if Revenue from Operations = ₹100

Gross Profit = ₹20

& Cost of Revenue from Operations = ₹80

If Cost of Revenue from Operations is ₹80, Revenue from Operations is ₹100

If Cost of Revenue from Operations is ₹4,00,000

Revenue from Operations is $\frac{100}{80} \times$ ₹ 4,00,000 = ₹5,00,000

$$\text{Working Capital Turnover Ratio} = \frac{\text{Revenue from Operations}}{\text{Working Capital}}$$

$$\text{or} \quad 10 = \frac{5{,}00{,}000}{\text{Working Capital}}$$

$$\text{Working Capital} = \frac{5{,}00{,}000}{10} = ₹50{,}000$$

Working Capital = Current Assets – Current Liabilities

or Current Assets = Working Capital + Current Liabilities

= ₹50,000 + ₹90,000

= ₹1,40,000

ILLUSTRATION 79.

From the following information, calculate :

(*i*) Revenue from Operations

(*ii*) Cost of Revenue from Operations

(*iii*) Working Capital

(*iv*) Current Assets

Trade Receivables Turnover Ratio	4 Times
Current Liabilities	₹5,000
Average Debtors	₹1,80,000
Working Capital Turnover Ratio	8 Times
Cash Revenue from Operations	25% of Revenue from Operations.
Gross Profit Ratio	$33\frac{1}{3}\%$

(I.S.C. Sample Question Paper, 2015)

SOLUTION :

$$(i)\ \text{Trade Receivables Turnover Ratio} = \frac{\text{Credit Revenue from Operations}}{\text{Average Trade Receivables}}$$

$$4\ (\text{Given}) = \frac{\text{Credit Revenue from Operations}}{1{,}80{,}000}$$

Credit Revenue from Operations = ₹1,80,000 × 4 = ₹7,20,000

Cash Revenue from Operations is 25% of Revenue from Operations

∴ Credit Revenue from Operations is 75% of Revenue from Operations

Revenue from Operations $= ₹7,20,000 \times \frac{100}{75} = ₹9,60,000$

(*ii*) Gross Profit is $33\frac{1}{3}\%$ of Revenue from Operations

Hence, Gross Profit $= 9,60,000 \times \frac{100}{3} \times \frac{1}{100} = 3,20,000$

Cost of Revenue from Operations = Revenue from Operations – Gross Profit

$= ₹9,60,000 - ₹3,20,000 = ₹6,40,000$

(*iii*) Working Capital Turnover Ratio $= \frac{\text{Revenue from Operations}}{\text{Working Capital}}$

Or $8 = \frac{9,60,000}{\text{Working Capital}}$

Working Capital $= \frac{9,60,000}{8} = ₹1,20,000$

(*iv*) Working Capital = Current Assets – Current Liabilities

or Current Assets = Working Capital + Current Liabilities

$= ₹1,20,000 + ₹5,000$

$= ₹1,25,000.$

ILLUSTRATION 80.

Calculate Working Capital Turnover Ratio from the following :

S. No.	*Items*	*Amount*
		₹
1.	Revenue from Operations (Sales)	12,00,000
2.	Current Assets	5,00,000
3.	Total Assets	8,00,000
4.	Non Current Liabilities	4,00,000
5.	Shareholder's Funds	2,00,000

SOLUTION :

Working Capital Turnover Ratio $= \frac{\text{Revenue from Operations}}{\text{Working Capital}}$

Revenue from Operations = ₹12,00,000

Working Capital = Current Assets – Current Liabilities

Current Assets = ₹5,00,000

Current Liabilities = Total Assets – Non Current Liabilities – Shareholder's Funds

$= ₹8,00,000 - ₹4,00,000 - ₹2,00,000$

$= ₹2,00,000$

Working Capital = ₹5,00,000 – ₹2,00,000 = ₹3,00,000

$$\text{Working Capital Turnover Ratio} = \frac{₹12,00,000}{₹3,00,000} = 4 \text{ Times}$$

ILLUSTRATION 81

A company earns Gross profit of 25% on cost. For the year ended 31st March, 2017 its Gross Profit was ₹5,00,000; Equity Share Capital of the company was ₹10,00,000; Reserves and Surplus ₹2,00,000; Long Term Loan ₹3,00,000 and Non Current Assets were ₹10,00,000

Compute the 'Working capital turnover ratio' of the company.

(C.B.S.E. 2018, Comptt.)

SOLUTION

Gross Profit is 25% of Cost

Hence. If Gross Profit is 25, Revenue from Operations = 125

If Gross Profit is ₹5,00,000, Revenue from Operations

$$= \frac{125}{25} \times 5,00,000 = ₹25,00,000$$

Working Capital = Equity Share Capital + Reserves & Surplus + Long Term Loan – Non Current Assets

= ₹10,00,000 + ₹2,00,000 + ₹3,00,000 – ₹10,00,000

= ₹5,00,000

$$\text{Working Capital Turnover Ratio} = \frac{\text{Revenue from Operations}}{\text{Working Capital}}$$

$$= \frac{25,00,000}{5,00,000} = 5 \text{ times}$$

ILLUSTRATION 82

Following particulars are given to you :

	31.3.2019 ₹	31.3.2020 ₹
Revenue from Operations	1,82,500	2,19,000
Cost of Revenue from Operations	1,42,500	1,69,000

BALANCE SHEETS

as at ....

	Note No.	31.3.2019 ₹	31.3.2020 ₹
I. EQUITY AND LIABILITIES :			
(1) Shareholder's Funds :			
(a) Share Capital		1,50,000	1,50,00
(b) Reserves & Surplus		30,000	40,00
(2) Non Current Liabilities :			
Long-term Borrowings		70,000	1,30,00

(3) Current Liabilities :			
Trade Payables		50,000	80,000
		3,00,000	4,00,000
II. ASSETS :			
(1) Non-Current Assets :			
Fixed Assets		2,10,000	2,08,000
(2) Current Assets :			
(*a*) Inventory		50,000	72,000
(*b*) Trade Receivables		30,000	60,000
(*c*) Cash and Bank Balance		5,000	50,000
(*d*) Other Current Assets (Prepaid Expenses)		5,000	10,000
		3,00,000	4,00,000

Calculate the following ratios :—

(I) Current Ratio; (II) Acid Test Ratio; (III) Trade Receivables Turnover Ratio; (IV) Working Capital Turnover Ratio; and (V) Inventory Turnover Ratio.

SOLUTION :

(I) Current Ratio $= \dfrac{\text{Current Assets}}{\text{Current Liabilities}}$

For 2019 $= \dfrac{\text{₹ } 50{,}000 + \text{₹ } 30{,}000 + \text{₹ } 5{,}000 + \text{₹}5{,}000}{\text{₹ } 50{,}000}$

$= \dfrac{\text{₹ } 90{,}000}{\text{₹ } 50{,}000} = 1.8 : 1$

For 2020 $= \dfrac{\text{₹ } 1{,}92{,}000}{\text{₹ } 80{,}000} = 2.4 : 1$

(II) Acid Test Ratio $= \dfrac{\text{Liquid Assets}}{\text{Current Liabilities}}$

For 2019 $= \dfrac{\text{₹ } 35{,}000}{\text{₹ } 50{,}000} = 0.7 : 1$

For 2020 $= \dfrac{\text{₹ } 1{,}10{,}000}{\text{₹ } 80{,}000} = 1.4 : 1$

(III) Trade Receivables Turnover Ratio $= \dfrac{\text{Revenue from Operations}}{\text{Average Trade Receivables}}$

For 2019 $= \dfrac{\text{Revenue from Operations}}{\text{Trade Receivables}}$

$= \dfrac{\text{₹ } 1{,}82{,}500}{\text{₹ } 30{,}000} = 6.08 \text{ Times}$

Average Trade Receivables for 2020 $= \dfrac{\text{₹ } 30{,}000 + \text{₹ } 60{,}000}{2} = \text{₹}45{,}000$

Trade Receivables Turnover Ratio $= \dfrac{\text{₹ } 2{,}19{,}000}{\text{₹ } 45{,}000} = 4.86 \text{ Times.}$

(IV) Working Capital Turnover Ratio $= \dfrac{\text{Revenue from Operations}}{\text{Working Capital}}$

Working Capital = Currest Assets – Current Liabilities

For 2019, Working Capital = ₹50,000 + ₹30,000 + ₹5,000 + ₹5,000 – ₹50,000

= ₹40,000

Working Capital Turnover Ratio $= \dfrac{₹\ 1{,}82{,}500}{₹\ 40{,}000} = 4.56$ times

For 2020, Working Capital = ₹72,000 + ₹60,000 + ₹50,000 + ₹10,000 – ₹80,000

= ₹1,12,000

Working Capital Turnover Ratio $= \dfrac{₹\ 2{,}19{,}000}{₹\ 1{,}12{,}000} = 1.96$ times

(V) Inventory Turnover Ratio $= \dfrac{\text{Cost of Revenue from Operations}}{\text{Average Inventory}}$

For 2019 $= \dfrac{1{,}42{,}500}{50{,}000} = 2.85$ Times

For 2020 Average Inventory $= \dfrac{₹\ 50{,}000 + ₹\ 72{,}000}{2}$

= ₹61,000

Inventory Turnover Ratio $= \dfrac{₹\ 1{,}69{,}000}{₹\ 61{,}000} = 2.77$ Times

(D) Profitability Ratios or Income Ratios

The main object of every business concern is to earn profits. A business must be able to earn adequate profits in relation to the capital invested in it. The efficiency and the success of a business can be measured with the help of profitability ratios. The following are the important profitability ratios :—

(*i*) Gross Profit Ratio
(*ii*) Operating Ratio
(*iii*) Net Profit Ratio
(*iv*) Operating Profit Ratio
(*v*) Earning Per Share
(*vi*) Price Earning Ratio
(*vii*) Return on Investment

(*i*) Gross Profit Ratio :—

This ratio establishes a relationship between gross profit and Revenue from Operations *i.e.*, Net Sales. This ratio is computed and presented in percentage. The formula for computing this ratio is :

$$\text{Gross Profit Ratio} = \frac{\text{Gross Profit}}{\text{Revenue from Operations } i.e., \text{ Net Sales}} \times 100$$

Gross Profit = Revenue from Operations – Cost of Revenue from Operations

Cost of Revenue from Operations = Opening Inventory + Net Purchases
+ Direct Expenses (Carriage, Wages etc.)
– Closing Inventory
OR Revenue from Operations – Gross Profit

It is to be noted that Spare Parts and Loose Tools are excluded from Inventory.

Objectives and Significance :— This ratio measures the margin of profit available on Revenue from Operations. The higher the gross profit ratio, the better it is. No ideal standard is fixed for this ratio, but the gross profit ratio should be adequate enough not only to cover the operating expenses but also to provide for depreciation, interest on loans, dividends and creation of reserves.

The ratio is compared with earlier years ratio and important conclusions are drawn from such comparison. For instance, if there is a decline in gross profit ratio in comparison to the previous year, it may be concluded that :

(I) Price of materials purchased, freight, wages and other direct charges may have gone up but the selling price may not have gone up in proportion to the increase in costs.

or (II) The selling prices may have fallen but the prices of materials, freight, wages and other direct charges may not have fallen relatively.

or (III) There may be misappropriation, theft or pilferage of inventory during the year.

or (IV) There is fall in the sale of more profitable varieties of goods.

or (V) There is fall in the prices of unsold goods, thereby reducing the value of closing inventory.

ILLUSTRATION 83.

Calculate Gross Profit Ratio from the following :

S.No.	*Items*	*Amount ₹*
1.	Opening Inventories	50,000
2.	Purchases	1,50,000
3.	Returns outwards	20,000
4.	Wages	10,000
5,	Revenue from Operations	2,50,000
6.	Closing Inventories	40,000

SOLUTION :

Gross Profit Ratio $= \dfrac{\text{Gross Profit}}{\text{Revenue from Operations}} \times 100$

Gross Profit = Revenue from Operations – Cost of Revenue from Operations

Cost of Revenue from Operations = Opening Inventories + Purchases – Returns Outwards + Wages – Closing Inventories
= ₹50,000 + ₹1,50,000 – ₹20,000 + ₹10,000 – ₹40,000
= ₹1,50,000

Gross Profit = ₹2,50,000 – ₹1,50,000 = ₹1,00,000

Gross Profit Ratio $= ₹\frac{1,00,000}{2,50,000} \times 100 = 40\%$

ILLUSTRATION 84.

Calculate the Gross Profit Ratio from the following information :—

	₹
Credit Revenue from Operations	3,00,000
Cash Revenue from Operations (being 25% of Total Revenue from Operations)	
Purchases	3,20,000
Excess of closing inventory over opening inventory	40,000

SOLUTION :

If total Revenue from Operations is ₹100,

Cash Revenue from Operations will be ₹25 & Credit Revenue from Operations ₹75.

Hence, If credit Revenue from Operations is ₹75 total sale will be = ₹100

If credit Revenue from Operations is ₹3,00,000 total

Revenue from Operations will be $= \frac{100}{75} \times 3,00,000 = ₹4,00,000$

Cost of Revenue from Operations = Purchases – Excess of Closing Inventory over Opening Inventory

= ₹3,20,000 – ₹40,000

= ₹2,80,000

Gross Profit = Total Revenue from Operations – Cost of Revenue from Operations

= ₹4,00,000 – ₹2,80,000 = ₹1,20,000

Gross Profit Ratio $= \frac{\text{Gross Profit}}{\text{Revenue from Operations}} \times 100$

$= \frac{₹1,20,000}{₹4,00,000} \times 100 = 30\%$

ILLUSTRATION 85.

Calculate Gross Profit Ratio from the following information :—

Cash Revenue from Operations was $\frac{1}{3}$rd of Total Revenue from Operations; Cash Revenue from Operations was ₹1,40,000;

Cash Purchase was 25% of Credit Purchase. Cash Purchase was ₹50,000.

Opening Inventory ₹30,000; Closing Inventory was ₹10,000 more than Opening Inventory. Carriage ₹12,000.

SOLUTION :

Step (*i*) If Cash Revenue from Operations is ₹1,

Total Revenue from Operations will be ₹3

If Cash Revenue from Operations is ₹1,40,000,

Total Revenue from Operations will be ₹1,40,000 × 3

= ₹4,20,000

Step *(ii)* If Cash Purchase is ₹25, Credit Purchase will be ₹100 and hence total Purchase will be ₹125

∴ If Cash Purchase is ₹25, Total Purchase = ₹125

If Cash Purchase is ₹50,000, Total Purchase $= \frac{125}{25} \times 50{,}000 =$ ₹2,50,000

Step *(iii)* Cost of Revenue from Operations

= Opening Inventory + Purchase + Carriage – Closing Inventory

$= 30{,}000 + 2{,}50{,}000 + 12{,}000 - 40{,}000 = 2{,}52{,}000$

Gross Profit = Total Revenue from Operations – Cost of Revenue from Operations

= ₹4,20,000 – ₹2,52,000 = ₹1,68,000

$$\text{Gross Profit Ratio} = \frac{\text{Gross Profit}}{\text{Revenue from Operations}} \times 100$$

$$= \frac{1{,}68{,}000}{4{,}20{,}000} \times 100 = 40\%$$

ILLUSTRATION 86.

Gross Profit of a Company is 25% of Cost of Revenue from Operations. Its credit Revenue from Operations are twice its cash Revenue from Operations. If the credit Revenue from Operations are ₹4,00,000, calculate the G.P. ratio.

SOLUTION :

Credit Revenue from Operations = ₹ 4,00,000

∴ Cash Revenue from Operations = ₹ 2,00,000

Hence, Total Revenue from Operations = ₹ 6,00,000

Gross profit is 25% of Cost of Revenue from Operations.

Therefore, goods costing ₹100 must have been sold for 125

Hence, If Revenue from Operations are ₹125, G.P. = ₹25

If Revenue from Operations are ₹6,00,000, G.P. $= 6{,}00{,}000 \times \frac{25}{125} =$ ₹1,20,000

$$\text{Gross Profit Ratio} = \frac{\text{Gross Profit}}{\text{Revenue from Operations}} \times 100 = \frac{1{,}20{,}000}{6{,}00{,}000} \times 100 = 20\%$$

ILLUSTRATION 87.

Following information is available for the year ending 31st March, 2020. Calculate Gross Profit Ratio :

		₹
Cash Revenue from Operations (Cash Sales)		2,00,000
Purchases :	Cash	1,50,000
	Credit	4,50,000
Carriage Inwards		6,000
Salaries		75,000
Decrease in Inventory		80,000
Return Outwards		20,000

Wages	50,000
Ratio of Cash Revenue from Operations and Credit Revenue from Operations	1 : 4

SOLUTION :

Revenue from Operations = Cash Revenue from Operations + Credit Revenue from Operations

$$= ₹2,00,000 + ₹2,00,000 \times \frac{4}{1}$$

$$= ₹2,00,000 + ₹8,00,000 = ₹10,00,000$$

Net Purchases = Cash Purchases + Credit Purchases – Return Outwards

$$= ₹1,50,000 + ₹4,50,000 - ₹20,000 = ₹5,80,000$$

Cost of Revenue from Operations = Purchases + (Opening Inventory – Closing Inventory) + Direct Expenses

= Purchases + Decrease in Inventory + Direct Expenses (*i.e.* Carriage Inwards + Wages)

$$= ₹5,80,000 + ₹80,000 + ₹6,000 + ₹50,000 = ₹7,16,000$$

Gross Profit = Revenue from Operations – Cost of Revenue from Operations

$$= ₹10,00,000 - ₹7,16,000 = ₹2,84,000$$

$$\text{Gross Profit Ratio} = \frac{\text{Gross Profit}}{\text{Revenue from Operations}} \times 100 = \frac{2,84,000}{10,00,000} \times 100 = 28.4\%$$

ILLUSTRATION 88.

Opening Inventory ₹60,000; Closing Inventory is 1.5 times of Opening Inventory Inventory Turnover Ratio 6 times; Selling price is $33\frac{1}{3}\%$ above cost. Calculate th Gross Profit ratio.

(C.B.S.E. 2020; Chennai, Mumba

SOLUTION :

Opening Inventory = ₹60,000

Closing Inventory = ₹60,000 × 1.5 = ₹90,000

$$\text{Average Inventory} = \frac{\text{Opening Inventory} + \text{Closing Inventory}}{2}$$

$$= \frac{60,000 + 90,000}{2} = ₹75,000$$

$$\text{Inventory Turnover Ratio} = \frac{\text{Cost of Revenue from Operations}}{\text{Average Inventory}}$$

$$6 = \frac{\text{Cost of Revenue from Operations}}{75,000}$$

Cost of Revenue from Operations = 75,000 × 6 = ₹4,50,000

Selling Price is $33\frac{1}{3}\%$ above cost

$$\therefore \text{Revenue from Operations} = 4,50,000 + 33\tfrac{1}{3}\% \text{ of } 4,50,000$$

$$= ₹4,50,000 + ₹1,50,000 = ₹6,00,000$$

$$\text{Gross Profit} = \text{Revenue from Operations} - \text{Cost of Revenue from Operations}$$

$$= ₹6{,}00{,}000 - ₹4{,}50{,}000 = ₹1{,}50{,}000$$

$$\text{Gross Profit Ratio} = \frac{\text{Gross Profit}}{\text{Revenue from Operations}} \times 100$$

$$= \frac{1{,}50{,}000}{6{,}00{,}000} \times 100 = 25\%$$

(*ii*) **Operating Ratio :**

This Ratio measures the proportion of an enterprise's cost of Revenue from Operations and operating expenses in comparison to its Revenue from Operations :

Operating Ratio =

$$\frac{\text{Cost of Revenue from Operations} + \text{Operating Expenses} - \text{Operating Income}}{\text{Revenue from Operations}} \times 100$$

where, Cost of Revenue from Operations = Opening Inventory + Net Purchases + Direct Exp. (Carriage, Wages etc.) – Closing Inventory

OR

Revenue from Operations – Gross Profit

Operating Expenses = Employee Benefit Exp. + Depreciation and Amortisation Expenses + Other Exp. (*i.e.* Office and Administration Exp. + Selling and Distribution Exp. + Discount + Bad-Debts + Interest on short-term loans).

Operating Income = Trading Commission received, cash discount received.

Attention : (1) Depreciation and Amortisation Expenses are included in Operating Expenses.

(2) Spare Parts and Loose Tools are excluded from Inventory.

It must be noted that non-operating expenses such as loss on sale of fixed assets, loss from fire, income tax, charities and donations, finance charges relating to interest on long-term debts and interest on debentures etc. are ignored while calculating this ratio. Similarly, non-operating incomes (such as profit on sale of fixed assets and interest and dividend received on investments) are also ignored.

Objectives and Significance : Operating Ratio is a measurement of the efficiency and profitability of the business enterprise. The ratio indicates the extent of Revenue from Operations that is absorbed by the cost of Revenue from Operations and operating expenses. Lower the operating ratio, the better it is, because it will leave higher margin of profit on Revenue from Operations.

ILLUSTRATION 89.

Calculate Operating Ratio from the following information :

	₹
Revenue from Operations	2,60,000
Revenue from Operations Return	10,000
Cost of Revenue from Operations	1,50,000

Selling Expenses	40,000
Administrative Expenses	20,000

SOLUTION :

Operating Expenses = Selling Expenses + Administrative Expenses

$$= ₹40,000 + ₹20,000 = ₹60,000$$

$$\text{Operating Ratio} = \frac{\text{Cost of Revenue from Operations + Operating Expenses}}{\text{Net Revenue from Operations}} \times 10$$

$$\frac{₹1,50,000 + ₹60,000}{₹2,60,000 - ₹10,000} \times 100 = \frac{2,10,000}{2,50,000} \times 100 = 84\%$$

ILLUSTRATION 90.

Calculate Operating Ratio from the following information :

	₹
Net Revenue from Operations	8,00,000
Cash Revenue from Operations	2,00,000
Gross Profit Ratio	20%
Office & Selling Expenses	60,000
Depreciation	20,000
Loss on Sale of Plant	10,000

SOLUTION :

$$\text{Operating Ratio} = \frac{\text{Cost of Revenue from Operations + Operating Expenses}}{\text{Net Revenue from Opertaions}} \times 1$$

Cost of Revenue from Operations = Net Revenue from Operations – Gross Profit

$$= ₹8,00,000 - 20\% \text{ of } 8,00,000$$

$$= ₹8,00,000 - ₹1,60,000 = ₹6,40,000$$

Operating Expenses = Office & Selling Expenses + Depreciation

$$= ₹60,000 + ₹20,000 = ₹80,000$$

$$\text{Hence, Operating Ratio} = \frac{₹6,40,000 + ₹80,000}{₹8,00,000} \times 100 = 90\%.$$

Note : Net Revenue from Operations means Credit Revenue from Operations + C Revenue from Operations – Revenue from Operations Return.

ILLUSTRATION 91.

From the following Statement of Profit and Loss of Yash Ltd. for the year en 31st March 2020, Compute Operating Ratio :

STATEMENT OF PROFIT AND LOSS

for the year ended 31st Marsh, 2020

Particulars	*Note No.*	₹
I. Revenue from Operations		16,00,0
II. *Add* : Other Incomes		40,0
III. Total Revenue I + II		16,40,0

IV. *Less* : Expenses		
Purchase of Stock-in-Trade		9,60,000
Changes in Inventories of Stock in Trade		(25,000)
Employee Benefit Expenses		1,80,000
Finance Costs		46,000
Depreciation and Amortization Expenses		40,000
Other Expenses	1	1,15,000
Total Expenses		13,16,000
V. Profit before Tax (III – IV)		3,24,000

Notes to Accounts :

Particulars	₹
1. Other Expenses :	
Administrative Expenses	70,000
Selling Expenses	31,000
Loss on Sale of Machinery	14,000
	1,15,000

$$\text{Operating Ratio} = \frac{\text{Cost of Revenue from Operations} + \text{Operating Expenses}}{\text{Revenue from Operations}} \times 100$$

Cost of Revenue from Operations = Purchase of Stock in Trade + Change in Inventory of Stock in Trade

= ₹9,60,000 – ₹25,000 = ₹9,35,000

Operating Expenses = Employee Benefit Exp. + Depreciation and Amortization Expenses + Other Exp. (*i.e.*, Administrative Exp. + Selling Exp.)

= ₹1,80,000 + ₹40,000 + ₹70,000 + ₹31,000

= ₹3,21,000

$$\text{Operating Ratio} = \frac{₹9{,}35{,}000 + ₹3{,}21{,}000}{₹16{,}00{,}000} \times 100$$

= 78.5%

ILLUSTRATION 92.

Operating Ratio	75%
Operating Expenses	₹ 40,000
Revenue from Operations	₹ 5,00,000
Revenue from Operations Return	₹ 20,000

Calculate Cost of Revenue from Operations.

SOLUTION :

Net Revenue from Operations = Revenue from Operations – Revenue from Operations Return

= ₹5,00,000 – ₹20,000 = ₹4,80,000

$$\text{Operating Ratio} = \frac{\text{Cost of Revenue from Operations + Operating Exp.}}{\text{Net Revenue from Operations}} \times 100$$

Hence, Cost of Revenue from Operations + Operating Exp.
= 75% of Net Revenue from Operations

Cost of Revenue from Operations + ₹40,000 = 75% of ₹4,80,000
Cost of Revenue from Operations = ₹3,60,000 – ₹40,000
= ₹3,20,000

(*iii*) Net Profit Ratio :

This ratio shows the relationship between net profit and revenue from operations. It may be calculated as follows :

$$\text{Net Profit Ratio} = \frac{\text{Net Profit after Tax}}{\text{Revenue from Operations}} \times 100$$

Net Profit = Gross Profit – Indirect Expenses & Losses + Other Incomes – Tax

Indirect Expenses & Losses = Office Exp. + Selling Exp. + Interest on Long term Borrowings + Accidental Losses

$$\textbf{(iv) Operating Profit Ratio} = \frac{\text{Operating Profit}}{\text{Revenue from Operations}} \times 100$$

Operating Profit = Gross Profit – Operating Exp. + Operating Incomes

Operating Exp. = Employee Benefit Exp., Depreciation, Office and Administrative Expenses, Selling and Distribution Expenses, Discount, Bad-debts, Interest on short term debts etc.

Operating Income = Commission Received + Discount Received

Operating Profit is arrived at by deducting operating expenses from gross profit, such as employee benefit exp., depreciation, office and administration expenses, selling and distribution expenses, Discount, Bad-debts, interest on short-term debts, etc. Non-operating expenses are not deducted from gross profit, such as loss on sale of non-current assets, loss from fire, income tax, charities and donations, finance charges relating to interest on long-term debts and interest on debentures etc. Similarly, non-operating incomes (such as profit on sale of non-current assets and income from investments) are also not added into gross profit.

It is important to note that if Net Profit is given in the question, Operating Profit may be calculated as follows :

Operating Profit = Net Profit (before Tax) + Non Operating Expenses/Losses – Non Operating Incomes

Note : 'Operating Ratio' and 'Operating Profit Ratio' are inter-related. Total of both these ratios will be 100. For example, if the 'Operating Ratio' is 80%, it means that the 'Operating Profit Ratio' is 20%. A rise in 'Operating Ratio' will lead to a similar amount of decline in 'Operating Profit Ratio' and vice versa.

ILLUSTRATION 93.

From the following calculate :

(*a*) Net Profit Ratio, (*b*) Operating Profit Ratio

S.No	Items	Amount ₹
1.	Revenue from Operations	2,00,000
2.	Gross Profit	75,000
3.	Office Expenses	15,000
4.	Selling Expenses	26,000
5.	Interest on Debentures	5,000
6.	Accidental losses	12,000
7.	Income from Rent	2,500
8.	Commission received	2,000

SOLUTION :

(*a*) Net Profit Ratio = $\dfrac{\text{Net Profit}}{\text{Revenue from Operations}} \times 100$

Net Profit = Gross Profit – Indirect Expenses & Losses + Other Incomes

Indirect Expenses and Losses = Office Expenses + Selling Expenses + Interest on Debentures + Accidental Losses
= ₹15,000 + ₹26,000 + ₹5,000 + ₹12,000
= ₹58,000

Other Incomes = Income from Rent + Commission Received
= ₹2,500 + ₹2,000 = ₹4,500

Net Profit = ₹75,000 – ₹58,000 + ₹4,500 = ₹21,500

Revenue from Operations = ₹2,00,000

∴ Net Profit Ratio = ₹ $\dfrac{21{,}500}{2{,}00{,}000} \times 100 = 10.75\%$

(*b*) Operating Profit Ratio = $\dfrac{\text{Operating Profit}}{\text{Revenue from Operations}} \times 100$

Operating Profit = Gross Profit + Operating Income – Operating Expenses

Operating Income = Commission Received
= ₹2,000

Operating Expenses = Office Expenses + Selling Expenses
= ₹15,000 + ₹26,000 = ₹41,000

∴ Operating Profit = ₹75,000 + ₹2,000 – ₹41,000 = ₹36,000

Revenue from Operations = ₹2,00,000

∴ Operating Profit Ratio = ₹ $\dfrac{36{,}000}{2{,}00{,}000} \times 100 = 18\%$

Objective and Significance : This ratio measures the rate of net profit earned on Revenue from Operations. It helps in determining the overall efficiency of the business operations. An increase in the ratio over the previous year shows improvement in the overall efficiency and profitability of the business.

ILLUSTRATION 94.

From the following, calculate Operating Profit Ratio :

	₹
Revenue from Operations	6,00,000
Cost of Revenue from Operations	4,00,000
Discount received	50,000
Selling Expenses	60,000
Interest on Debentures	30,000

(I.S.C. Specimen Question Paper, 2018)

SOLUTION :

$$\text{Operating Profit Ratio} = \frac{\text{Operating Profit}}{\text{Revenue from Operations}} \times 100$$

Operating Profit = Gross Profit + Operating Income – Operating Expenses

Gross Profit = Revenue from Operations – Cost of Revenue from Operations

= ₹6,00,000 – ₹4,00,000 = ₹2,00,000

Operating Income = Discount Received ₹50,000

Operating Expenses = Selling Expenses ₹60,000

Operating Profit = ₹2,00,000 + ₹50,000 – ₹60,000

= ₹1,90,000

$$\text{Operating Profit Ratio} = ₹\frac{1,90,000}{6,00,000} \times 100 = 31.67\%$$

ILLUSTRATION 95.

Calculate (*i*) G.P. Ratio, (*ii*) Operating Ratio, (*iii*) Operating Profit Ratio and (*iv*) Net Profit Ratio from the following :

	₹
Opening Inventory	3,00,000
Closing Inventory	4,20,000
Purchases	14,00,000
Wages	3,70,000
Carriage Inwards	1,50,000
Administrative Exp.	84,000
Selling Exp.	36,000
Income Tax	1,00,000
Profit on Sale of Fixed Assets	20,000
Revenue from Operations	24,00,000

SOLUTION :

$$(i)\ \text{Gross Profit Ratio} = \frac{\text{Gross Profit}}{\text{Revenue from Operations}} \times 100$$

Gross Profit = Revenue from Operations – Cost of Revenue from Operations

= Revenue from Operations – (Opening Inventory + Purchases + Wages + Carriage Inwards – Closing Inventory)

$$= 24{,}00{,}000 - (3{,}00{,}000 + 14{,}00{,}000 + 3{,}70{,}000 + 1{,}50{,}000 - 4{,}20{,}000)$$

$$= 24{,}00{,}000 - 18{,}00{,}000 = 6{,}00{,}000.$$

$$\text{G.P. Ratio} = \frac{6{,}00{,}000}{24{,}00{,}000} \times 100 = 25\%$$

(*ii*) $$\text{Operating Ratio} = \frac{\text{Cost of Revenue from Operations} + \text{Operating Exp.}}{\text{Revenue from Operations}} \times 100$$

Operating Exp. = Administrative Exp. + Selling Exp.

= 84,000 + 36,000 = 1,20,000

$$\text{Operating Ratio} = \frac{18{,}00{,}000 + 1{,}20{,}000}{24{,}00{,}000} \times 100 = 80\%$$

(*iii*) $$\text{Operating Profit Ratio} = \frac{\text{Operating Profit}}{\text{Revenue from Operations}} \times 100$$

Operating Profit = G.P. – Operating Exp. (*i.e.* Administrative Exp. and Selling Exp.)

= 6,00,000 – 84,000 – 36,000 = 4,80,000

$$\text{Operating Profit Ratio} = \frac{4{,}80{,}000}{24{,}00{,}000} \times 100 = 20\%$$

(*iv*) $$\text{Net Profit Ratio} = \frac{\text{Net Profit}}{\text{Revenue from Operations}} \times 100$$

Net Profit = G.P. – Administrative Exp. – Selling Exp. – Income Tax + Profit on sale of fixed assets

= 6,00,000 – 84,000 – 36,000 – 1,00,000 + 20,000

= 4,00,000

$$\text{Net Profit Ratio} = \frac{4{,}00{,}000}{24{,}00{,}000} \times 100 = 16.67\%$$

ILLUSTRATION 96.

Gross Profit Ratio of a Company was 20%. Its credit Revenue from Operations were ₹18,00,000 and its cash Revenue from Operations were 10% of the total Revenue from Operations. If the indirect expenses of the Company were ₹50,000, calculate its net profit ratio.

SOLUTION :

Cash Revenue from Operations were 10% of total Revenue from Operations.

It means credit Revenue from Operations were 90% of total Revenue from Operations.

If credit Revenue from Operations were 90, total Revenue from Operations were 100.

If credit Revenue from Operations were ₹18,00,000, total Revenue from Operations were : $\frac{100}{90} \times 18{,}00{,}000 = ₹20{,}00{,}000$

Gross Profit $= ₹20,00,000 \times \frac{20}{100} = ₹4,00,000$

Net Profit = Gross Profit – Indirect Expenses

= ₹4,00,000 – ₹50,000

= ₹3,50,000

$$\text{Net Profit Ratio} = \frac{\text{Net Profit}}{\text{Revenue from Operations}} \times 100$$

$$= \frac{3,50,000}{20,00,000} \times 100 = 17.5\%$$

ILLUSTRATION 97.

Calculate Net Profit Ratio from the following information :

Revenue from Operations (Sales) ₹20,00,000; Gross Profit Ratio 30%; Operating Ratio 80%; Non-Operating Expenses ₹30,000; Non-operating Income ₹50,000.

SOLUTION :

$$\text{Net Profit Ratio} = \frac{\text{Net Profit}}{\text{Revenue from Operations}} \times 100$$

(*i*) Operating Profit Ratio = 100 – Operating Ratio

= 100 – 80 = 20%

(*ii*) Operating Profit $= ₹20,00,000 \times \frac{20}{100} = ₹4,00,000$

(*iii*) Net Profit = Operating Profit – Non Operating Exp. + Non Operating Income

= ₹4,00,000 – ₹30,000 + ₹50,000

= ₹4,20,000

(*iv*) Net Profit Ratio $= \frac{₹4,20,000}{₹20,00,000} \times 100 = 21\%$

CASE BASED MCQs — 6

Particulars	₹
Net Revenue from Operations	25,00,000
Credit Revenue from Operations	15,00,000
Gross Profit	40%
Employee Benefit Exp.	2,00,000
Depreciation	50,000
Selling Expenses	1,00,000
Interest on Long term Debts	3,00,000

(*a*) Operating Ratio will be :

(*i*) 68.75%
(*ii*) 72%
(*iii*) 86%
(*iv*) 74%

(*b*) Operating Profit Ratio will be :

(*i*) 26% (*ii*) 28%

(*iii*) 31.25% (*iv*) 14%

(See Answers at the end of the book)

(*v*) **Earning Per Share (E.P.S.) :—** Overall profitability of a Company can also be judged by calculating 'earning per share'. In this context, earnings refer to profit available for equity shareholders. This ratio is calculated with the help of the following formula :—

Earning Per Share (E.P.S.)

$$= \frac{\text{Net Profit (After Interest, Tax and Dividend on Preference Shares)}}{\text{Number of Equity Shares}}$$

Objectives and Significance :— This ratio is helpful in the determination of the market price of the equity share of the company. The ratio is also helpful in estimating the capacity of the company to declare dividends on equity shares.

(*vi*) **Price-Earning (P.E.) Ratio :** It is computed by dividing the market price of an equity share by the E.P.S. That is,

$$\text{P.E. Ratio} = \frac{\text{Market Price of the Equity Share}}{\text{E.P.S.}}$$

This ratio shows how much is to be invested in the market in this company's shares to get each ₹ of earning on its shares. The ratio is used to measure whether the market price of a share is high or low.

ILLUSTRATION 98.

Calculate the (*i*) Earning Per Share and (*ii*) Price Earning Ratio from the following data :

	₹
Net Profit before Tax	1,44,000
Tax Rate	50%
20,000 Equity Shares of ₹10 each	2,00,000
12% Preference Share Capital	1,00,000
Market Price of Equity Share	36

SOLUTION :

	₹
Net Profit before Tax	1,44,000
Less : Tax @ 50%	72,000
Profit after Tax	72,000
Less : Preference Dividend (12% on ₹1,00,000)	12,000
Profit available to Equity Shareholders	60,000

(*i*) Earning Per Share (E.P.S.) $= \frac{\text{Net Profit after Tax and Preference Dividend}}{\text{Number of Equity Shares}}$

$= \frac{₹\ 60,000}{20,000} = ₹3$ per share (*ii*) Price Earning (P.E.) Ratio $= \dfrac{\text{Market Price of the Equity Share}}{\text{E.P.S.}}$

$= \dfrac{₹36}{₹3} = 12$ times

ILLUSTRATION 99.

Your company has the following earnings last year :

Profit before Tax	₹20,00,000
Tax rate	35%

Capital :

(*a*) Equity shares 30,000 shares of ₹100 each	₹30 lakh
(*b*) 10% Preference Shares	₹10 lakh

From the above calculate (*i*) Earning per share and (*ii*) Price Earning Ratio The current market price of the equity share is ₹200.

SOLUTION :

Earning Per Share (E.P.S.) $= \dfrac{\text{Net Profit after Tax and Preference Dividend}}{\text{Number of Equity Shares}}$

Profit before Tax	=	20,00,000
Less : Tax @ 35%	=	7,00,000
Profit after tax (PAT)		13,00,000
Less : Preference Dividend (@ 10% on ₹10 Lakhs)		1,00,000
Net Profit after tax and Preference Dividend		12,00,000

(*i*) Earning Per Share $= \dfrac{12{,}00{,}000}{30{,}000} = ₹40$

(*ii*) Price Earning Ratio $= \dfrac{\text{Market Price of the Equity Share}}{\text{E.P.S.}}$

$= \dfrac{₹200}{₹40} = 5$ times

vii) Return on Investment or R.O.I. :

This ratio reflects the overall profitability of the business. It is calculated by omparing the profit earned and the capital employed to earn it. This ratio is usually in ercentage and is also known as **'Rate of Return'** or **'Return on Capital Employed'** r **'Yield on Capital'**.

The term 'Investment' here refers to long-term funds deployed in the enterprise. s defined earlier long-term funds are also known as capital employed which means otal of shareholders funds and long-term loans.

The ratio is computed as under :

$$\text{Return on Investment} = \frac{\text{Net Profit before Interest, Tax and Dividends}}{\text{Capital Employed}} \times 100$$

Since the Capital employed includes shareholder's funds and long-term loans, nterest paid on long-term loans will not be deducted from profits while calculating this atio.

Capital employed can be computed by any of the following two methods :

First Method (Liabilities Side Approach) :

Capital Employed = Shareholder's Funds + Non Current Liabilities i.e. (Long term Borrowings + Long term Provisions) (–) Non Trade Investments

Second Method (Assets Side Approach) :

Capital Employed = Non Current Assets (excluding Non-trade investments) + Working Capital

OR

Capital Employed = Fixed Assets + Trade Investments + Working Capital

ILLUSTRATION 100.

Following is the Balance Sheet of *X* Ltd. as at 31st March, 2018 :

Particulars	*Note No.*	₹
I. EQUITY AND LIABILITIES :		
Shareholder's Funds :		
(*a*) Share Capital		2,00,000
(*b*) Reserves & Surplus	1	70,000
Non-Current Liabilities :		
Long-term Borrowings	2	1,00,000
Long-term Provisions		30,000
Current Liabilities		1,80,000
TOTAL		5,80,000
II. ASSETS :		
Non-Current Assets		3,40,000
Current Assets		2,40,000
TOTAL		5,80,000

Notes : (1) Reserve & Surplus :

	₹
Reserve	5,000
Profit for the year	65,000
	70,000

(2) Long-term Borrowings :

15% Debentures	1,00,000

Calculate the 'Return on Investment'.

OLUTION :

$$\text{Return on Investment} = \frac{\text{Net Profit before Interest and Tax}}{\text{Capital Employed}} \times 100$$

Calculation of Net Profit before Interest & Tax	₹
Profit as per Balance Sheet	65,000

Add : Interest on Debentures (15% on ₹1,00,000)	15,000
Net Profit before Interest & Tax	80,000

Capital Employed (First Method) :

Share Capital	2,00,000
Reserve	5,000
Profit for the year	65,000
15% Debentures	1,00,000
Long-term Provision	30,000
Capital Employed	4,00,000

Capital Employed (Second Method) :

Non Current Assets	3,40,000
Add : Working Capital (Current Assets ₹2,40,000 *less* Current Liabilities ₹1,80,000)	60,000
Capital Employed	4,00,000

$$\text{Return on Investment} = \frac{\text{Net Profit before Interest and Tax}}{\text{Capital Employed}}$$

$$= \frac{80{,}000}{4{,}00{,}000} \times 100 = 20\%$$

Objectives and Significance : Since profit is the overall objective of a business enterprise, this ratio is a barometer of the overall performance of the enterprise. It measures how efficiently the capital employed in the business is being used. In other words, it is also a measure of the earning power of the net assets of the business. Even the performance of two dissimilar firms may be compared with the help of this ratio.

Furthermore, the ratio can be used to judge the borrowing policy of the enterprise. If an enterprise having the ratio of return on investment of 15%, borrows at 16%, it would indicate that it is borrowing at a rate higher than its earning rate.

ILLUSTRATION 101.

From the following calculate Return on Investment (or Return on Capital Employed)

S. No.	*Items*	*Amount*
		₹
1.	Share Capital	50,000
2.	Reserves & Surplus	25,000
3.	Fixed Assets	2,10,000
4.	Trade Investments	15,000
5.	Non Trade Investments	25,000
6.	Current Assets	1,10,000
7.	12% Long term borrowings	2,00,000
8.	Current Liabilities	85,000

Net Profit before Tax ₹60,000.

SOLUTION :

Return on Investment or Return on Capital Employed

$$= \frac{\text{Net Profit before Interest and Tax}}{\text{Capital Employed}} \times 100$$

		₹
Net Profit before Tax	=	60,000
Add : Interest : 12% on ₹2,00,000	=	24,000
Net Profit before Interest and Tax	=	84,000

Capital Employed (Liability Side Approach) = Share Capital + Reserves & Surplus + 12% long term borrowings – Non trade Investments

= ₹50,000 + ₹25,000 + ₹2,00,000 – ₹25,000

= ₹2,50,000

OR

Capital Employed (Assets Side Approach) = Fixed Assets + Trade Investments + Working Capital (*i.e.*, Current Assets – Current Liabilities)

= ₹2,10,000 + ₹15,000 + ₹1,10,000 – ₹85,000

= ₹2,50,000

Therefore, Return on Investment or Return on Capital Employed

$$= \frac{₹84,000}{₹2,50,000} \times 100 = 33.6\%$$

ILLUSTRATION 102.

Net Profit after Interest but before tax ₹1,40,000; 15% Long-term debts ₹4,00,000; Shareholder's funds ₹2,40,000; Tax rate 50%. Calculate Return on Capital Employed.

SOLUTION :

$$\text{Return on Capital Employed} = \frac{\text{Net Profit before Interest and Tax}}{\text{Capital Employed}} \times 100$$

Calculation of Profit before interest and tax :

Net Profit after Interest but before Tax	₹	1,40,000
+ Interest (15% on ₹4,00,000)	₹	60,000
Net Profit before Interest and Tax	₹	2,00,000

Capital Employed = Shareholder's Funds + Long-term Debts

= ₹2,40,000 + ₹4,00,000 = ₹6,40,000

$$\text{Return on Capital Employed} = \frac{2,00,000}{6,40,000} \times 100 = 31.25\%$$

Note : It is assumed that Shareholder's Funds include current year's profits.

ILLUSTRATION 103.

Net profit after Interest and Tax ₹1,00,000; Current assets ₹4,00,000; Current liabilities ₹2,00,000; Tax rate 20%; Fixed assets ₹6,00,000; 10% Long term Debt ₹4,00,000.

Calculate Return on Investment. *(C.B.S.E. 2017, 2018 Comptt.)*

SOLUTION :

$$\text{Return on Investment} = \frac{\text{Net Profit before Interest and Tax}}{\text{Capital employed}} \times 100$$

Calculation of Net Profit before Interest and Tax =

Net Profit after Tax = ₹1,00,000

$$\text{Net Profit before Tax} = 1{,}00{,}000 \times \frac{100}{80} = \text{₹}1{,}25{,}000$$

Net profit before Interest and Tax = ₹1,25,000 + Interest ₹40,000
= ₹1,65,000

Capital Employed = Fixed Assets + Current Assets – Current Liabilities
= ₹6,00,000 + ₹4,00,000 – ₹2,00,000
= ₹8,00,000

$$\text{Return on Investment} = \frac{1{,}65{,}000}{8{,}00{,}000} \times 100 = 20.625\%$$

ILLUSTRATION 104.

From the following details, calculate 'Return on Capital Employed' :

Gross Profit ₹1,00,000; Office and Administrative Expenses ₹10,000; Selling and Distribution Expenses ₹25,000; Interest on Long-term Debts ₹8,000; Tax ₹12,000; Non Current Assets ₹3,00,000; Current Assets ₹1,50,000 and Current Liabilities ₹1,25,000.

SOLUTION :

$$\text{Return on Capital Employed} = \frac{\text{Net Profit before Interest and Tax}}{\text{Capital Employed}} \times 100$$

Net Profit before Interest and Tax = Gross Profit – Office and Administrative Exp. – Selling and Distribution Exp.
= ₹1,00,000 – ₹10,000 – ₹25,000 = ₹65,000

Capital Employed = Non Current Assets + Current Assets – Current Liabilities
= ₹3,00,000 + ₹1,50,000 – ₹1,25,000
= ₹3,25,000

$$\text{Return on Capital Employed} = \frac{65{,}000}{3{,}25{,}000} \times 100 = 20\%$$

ILLUSTRATION 105.

Calculate Return on Investment Ratio and Inventory Turnover Ratio from the figures given below :

	₹
Opening Inventory	30,000
Closing Inventory	40,000
Carriage Inwards	10,000
Purchases	1,00,000
Current Assets	50,000

Current Liabilities	20,000
Non Current Assets	80,000
Indirect Expenses	15,000
Revenue from Operations	2,00 000

SOLUTION :

(I) Return on Investment = $\dfrac{\text{Net Profit before Interest and Tax}}{\text{Capital Employed}} \times 100$

Net Profit before Interest = Gross Profit – Indirect Expenses

Gross Profit = Revenue from Operations – Cost of Revenue from Operations

Cost of Revenue from Operations

= Opening Inventory + Purchases + Carriage Inwards – Closing Inventory

= 30,000 + 1,00,000 + 10,000 – 40,000 = ₹1,00,000

Gross Profit = 2,00,000 – 1,00,000 = 1,00,000

Net Profit before Interest = Gross Profit – Indirect Expenses

= 1,00,000 – 15,000 = 85,000

Capital Employed = Non Current Assets + Current Assets – Current Liabilities

= 80,000 + 50,000 – 20,000

= ₹1,10,000

Return on Investment = $\dfrac{85,000}{1,10,000} \times 100 = 77.27\%$

(II) Inventory Turnover Ratio= $\dfrac{\text{Cost of Revenue from Operations}}{\text{Average Inventory}}$

Average Inventory = $\dfrac{30,000 + 40,000}{2}$ = ₹35,000

Inventory Turnover Ratio= $\dfrac{1,00,000}{35,000}$ = 2.86 times

ILLUSTRATION 106.

From the following details, calculate Return on Investment :

	₹
Share Capital :	
Equity	4,00,000
Preference	1,00,000
General Reserve	2,70,000
10% Debentures	4,00,000
Current Liabilities	1,00,000
Net Profit (after Debenture interest and Income Tax)	80,000
Rate of Tax	50%

SOLUTION :

Return on Investment = $\dfrac{\text{Net Profit before Interest and Tax}}{\text{Capital Employed}} \times 100$

Calculation of Net Profit before Interest and Tax :

Net Profit after Tax = ₹80,000

Net Profit before Tax $= ₹80{,}000 \times \frac{100}{50} = ₹1{,}60{,}000$

Net Profit before Interest and Tax = ₹1,60,000 + Interest ₹40,000
= ₹2,00,000

Capital Employed = Shareholder's Funds + Non Current Liabilities
= Equity Capital + Pref. Capital
+ General Reserve + Current year's Profit
+10% Debentures
= ₹4,00,000 + ₹1,00,000 + ₹2,70,000
+ ₹80,000 + ₹4,00,000
= ₹12,50,000

$$= \frac{₹2{,}00{,}000}{₹12{,}50{,}000} \times 100 = 16\%$$

Note : It should be remembered that Current Year's profit is also added while calculating the capital employed from first method, *i.e.*, on the basis of share capital.

ILLUSTRATION 107.

A company has a loan of ₹20,00,000 as part of its capital employed. The interest payable on loan is 15% and the ROI of the company is 25%. The rate of income tax is 40%. What is the gain to the shareholders due to the loan raised by the company?

SOLUTION :

$$\text{Return on Investment (R.O.I.)} = \frac{\text{Net Profit before Interest and Tax}}{\text{Capital Employed}} \times 100$$

Since Capital Employed given in the question is ₹20,00,000 and R.O.I. is 25%, therefore :

		₹
Net Profit before Interest and Tax $= 20{,}00{,}000 \times \frac{25}{100}$	=	5,00,000
Less : Interest paid 15% of ₹20,00,000	=	3,00,000
Profit after Interest		2,00,000
Less : Tax paid 40% of ₹2,00,000	=	80,000
Net gain to shareholders :		1,20,000

ILLUSTRATION 108.

Calculate the following ratios from the details given below :

(*i*) Current Ratio
(*ii*) Liquid Ratio
(*iii*) Operating Ratio
(*iv*) Gross Profit Ratio

Details :

Current Assets = ₹70,000
Net working capital = ₹30,000
Inventories = ₹30,000
Revenue from Operations = ₹1,40,000
Cost of Revenue from Operations = ₹ 68,000

SOLUTION :

(*i*) Current Ratio

$$\text{Current Ratio} = \frac{\text{Current Assets}}{\text{Current Liabilities}}$$

$$\text{Current Liabilities} = \text{Current Assets} - \text{Net Working Capital}$$

$$= ₹70{,}000 - ₹30{,}000 = ₹40{,}000$$

$$\text{Current Ratio} = \frac{₹70{,}000}{₹40{,}000} = 1.75 : 1$$

(*ii*) Liquid Ratio

$$\text{Liquid Ratio} = \frac{\text{Liquid Assets}}{\text{Current Liabilities}}$$

$$\text{Liquid Assets} = \text{Current Assets} - \text{Inventories}$$

$$= ₹70{,}000 - ₹30{,}000 = ₹40{,}000$$

$$\text{Liquid Ratio} = \frac{₹40{,}000}{₹40{,}000} = 1 : 1$$

(*iii*) Operating Ratio

$$\text{Operating Ratio} = \frac{\text{Cost of Revenue from Operations} + \text{Operating Exp.}}{\text{Revenue from Operations}} \times 100$$

$$= \frac{68{,}000}{1{,}40{,}000} \times 100 = 48.57\%$$

(*iv*) Gross Profit Ratio

$$\text{Gross Profit Ratio} = \frac{\text{Gross Profit}}{\text{Revenue from Operations}} \times 100$$

$$\text{Gross Profit} = \text{Revenue from Operations} - \text{Cost of Revenue from Operations}$$

$$= 1{,}40{,}000 - 68{,}000 = 72{,}000$$

$$\text{Gross Profit Ratio} = \frac{72{,}000}{1{,}40{,}000} \times 100 = 51.43\%$$

ILLUSTRATION 109.

Calculate any three of the following ratios with the help of the information given below :

(*i*) Operating Ratio
(*ii*) Gross Profit Ratio
(*iii*) Quick Ratio
(*iv*) Working Capital Turnover Ratio
(*v*) Proprietary Ratio

Information :

Equity Share Capital ₹1,00,000; 8% Preference Share Capital ₹80,000; Long-term Borrowings (9% Debentures ₹60,000); Reserve and Surplus ₹10,000; Revenue from Operations ₹2,00,000; Opening Inventory ₹12,000; Purchases ₹1,20,000; Wages ₹8,000; Closing Inventory ₹18,000; Selling and Distribution Expenses ₹2,000; Liquid Assets ₹50,000, Tangible Fixed Assets ₹2,12,000 and Current Liabilities ₹30,000.

SOLUTION :

(*i*) Operating Ratio =

$$\frac{\text{Cost of Revenue from Operations} + \text{Operating Expenses}}{\text{Net Revenue from Operations}} \times 100$$

Cost of Revenue from Operations = Opening Inventory + Purchases + Wages – Closing Inventory

$$= \text{₹}12{,}000 + \text{₹}1{,}20{,}000 + \text{₹}8{,}000 - \text{₹}18{,}000$$

$$= \text{₹}1{,}22{,}000.$$

$$\text{Operating Ratio} = \frac{\text{₹}1{,}22{,}000 + \text{₹}2{,}000 \text{ (Selling Exp.)}}{\text{₹}2{,}00{,}000} \times 100 = 62\%$$

$$\text{(ii) Gross Profit Ratio} = \frac{\text{Gross Profit}}{\text{Net Revenue from Operations}} \times 100$$

Gross Profit = Net Revenue from Operations – Cost of Revenue from Operations

$$= \text{₹}2{,}00{,}000 - \text{₹}1{,}22{,}000 = \text{₹}78{,}000$$

$$\text{Gross Profit Ratio} = \frac{\text{₹}78{,}000}{\text{₹}2{,}00{,}000} \times 100 = 39\%$$

$$\text{(iii) Quick Ratio} = \frac{\text{Liquid Assets}}{\text{Current Liabilities}}$$

$$= \frac{\text{₹}50{,}000}{\text{₹}30{,}000} = 1.67 : 1$$

$$\text{(iv) Working Capital Turnover Ratio} = \frac{\text{Net Revenue from Operations}}{\text{Working Capital}}$$

Working Capital = Closing Inventory + Liquid Assets – Current Liabilities

$$= \text{₹}18{,}000 + \text{₹}50{,}000 - \text{₹}30{,}000 = \text{₹}38{,}000$$

$$\text{Working Capital Turnover Ratio} = \frac{\text{₹}2{,}00{,}000}{\text{₹}38{,}000} = 5.26 \text{ times}$$

$$\text{(v) Proprietary Ratio} = \frac{\text{Shareholder's Funds}}{\text{Total Assets}}$$

Shareholder's Funds = Equity Share Capital + Preference Share Capital + Reserve and Surplus*

$$= \text{₹}1{,}00{,}000 + \text{₹}80{,}000 + \text{₹}10{,}000$$

$$= \text{₹}1{,}90{,}000$$

Total Assets = Closing Inventory + Liquid Assets + Tangible Fixed Assets

$$= \text{₹}18{,}000 + \text{₹}50{,}000 + \text{₹}2{,}12{,}000 = \text{₹}2{,}80{,}000$$

$$\text{Proprietary Ratio} = \frac{\text{₹}1{,}90{,}000}{\text{₹}2{,}80{,}000} \times 100 = 67.86\%$$

Reserve and Surplus includes current year's Net Profit also.

ILLUSTRATION 110.

From the following information, calculate the following ratios (up to two decimal places) :

(*i*) Debt-Equity Ratio
(*ii*) Interest Coverage Ratio
(*iii*) Proprietary Ratio

	Amount ₹
Equity Share Capital	2,00,000
5% Preference Share Capital	60,000
General Reserve	1,20,000
Fixed Assets	5,05,000
Current Assets	1,20,000
Current Liabilities	40,000
Loan @ 10% interest	5,00,000
Tax paid during the year	30,000
Profit for the current year after interest and tax (available for the shareholders)	90,000

(I.S.C. 2014)

SOLUTIONS :

(*i*) Debt Equity Ratio = $\frac{\text{Debt}}{\text{Equity}}$ or $\frac{\text{Long Term Debts}}{\text{Shareholder's Funds}}$

Debt = Loan *i.e.* ₹5,00,000

Shareholder's Funds = Equity Share Capital + Pref. Share Capital + General Reserve + Profit for the Current year
= ₹2,00,000 + ₹60,000 + ₹1,20,000 + ₹90,000
= ₹4,70,000

Debt Equity Ratio = $\frac{5,00,000}{4,70,000} = 1.06 : 1$

(*ii*) Interest Coverage Ratio = $\frac{\text{Net Profit before Interest and Income Tax}}{\text{Fixed Interest Charges}}$

Fixed Interest Charges = 10% Interest on Loan of ₹5,00,000
= ₹50,000

Net Profit before Interest and Tax = Profit after Interest and Tax + Interest + Tax
= ₹90,000 + ₹50,000 + ₹30,000 = ₹1,70,000

Interest Coverage Ratio = $\frac{1,70,000}{50,000} = 3.4$ times.

(*iii*) Proprietary Ratio = $\frac{\text{Equity}}{\text{Total Assets}}$ or $\frac{\text{Shareholder's Funds}}{\text{Total Assets}}$

Total Assets = Fixed Assets + Current Assets
= ₹5,05,000 + ₹1,20,000 = ₹6,25,000

Proprietary Ratio = $\frac{4,70,000}{6,25,000} = 0.752 : 1$

ILLUSTRATION 111.

Calculate the following ratios from the given information :

(*i*) Working Capital Turnover Ratio
(*ii*) Debt-Equity Ratio
(*iii*) Gross Profit Ratio
(*iv*) Operating Ratio
(*v*) Current Ratio

Information :

Particulars	₹
Net Revenue from Operations	2,00,000
Cost of Revenue from Operations	1,20,000
Operating Expenses	30,000
Current Assets	60,000
Current Liabilities	30,000
Capital Employed	2,40,000
Long-term Debts	1,60,000

(*I.S.C. 2006*)

SOLUTION :

(*i*) $$\text{Working Capital Turnover Ratio} = \frac{\text{Net Revenue from Operations}}{\text{Working Capital}}$$

$$\begin{aligned}\text{Working Capital} &= \text{Current Assets} - \text{Current Liabilities}\\ &= ₹60{,}000 - ₹30{,}000\\ &= ₹30{,}000\end{aligned}$$

$$\text{Working Capital Turnover Ratio} = \frac{2{,}00{,}000}{30{,}000} = 6.67 \text{ times}$$

(*ii*) $$\text{Debt Equity Ratio} = \frac{\text{Debt}}{\text{Equity}} \text{ or } \frac{\text{Long Term Debts}}{\text{Shareholder's Funds}}$$

Capital employed is given in the question. It includes shareholder's Funds and long term debts. Hence,

$$\begin{aligned}\text{Shareholder's Funds} &= \text{Capital Employed} - \text{Long Term Debts}\\ &= 2{,}40{,}000 - 1{,}60{,}000 = 80{,}000.\end{aligned}$$

$$\text{Debt Equity Ratio} = \frac{1{,}60{,}000}{80{,}000} = 2:1$$

(*iii*) $$\text{Gross Profit Ratio} = \frac{\text{Gross Profit}}{\text{Net Revenue from Operations}} \times 100$$

$$\begin{aligned}\text{Gross Profit} &= \text{Net Revenue from Operations} - \text{Cost of Revenue from Operations}\\ &= 2{,}00{,}000 - 1{,}20{,}000 = 80{,}000\end{aligned}$$

$$\text{Gross Profit Ratio} = \frac{80{,}000}{2{,}00{,}000} \times 100 = 40\%$$

(*iv*) Operating Ratio

$$= \frac{\text{Cost of Revenue from Operations} + \text{Operating Expenses}}{\text{Net Revenue from Operations}} \times 100$$

$$= \frac{1,20,000 + 30,000}{2,00,000} \times 100 = 75\%$$

(*v*) Current Ratio

$$= \frac{\text{Current Assets}}{\text{Current Liabilities}}$$

$$= \frac{60,000}{30,000} = 2:1$$

ILLUSTRATION 112.

Calculate the following ratios from the given information :

(*i*) Acid Test Ratio
(*ii*) Gross Profit Ratio
(*iii*) Inventory Turnover Ratio
(*iv*) Debt Equity Ratio

Particulars		*Amount*
		₹
Revenue from Operations (Sales)		5,00,000
Less : Purchases	2,00,000	
Changes in Inventories (Opening Inventory – Closing Inventory) (50,000 – 80,000)	(–) 30,000	
Direct Expenses	50,000	2,20,000
Gross Profit		2,80,000

BALANCE SHEET
as at 31st March, 2018

Particulars	*Note No.*	₹
I. EQUITY AND LIABILITIES :		
(1) Shareholder's Funds :		
(*a*) Share Capital	1	7,00,000
(*b*) Reserves & Surplus	2	1,11,000
(2) Non-Current Liabilities :		
Long Term Borrowings		1,50,000
(3) Current Liabilities :		
Trade Payables		24,000
TOTAL		9,85,000
II. ASSETS :		
(1) Non-Current Assets :		
Fixed Assets		7,20,000
(2) Current Assets :		
(*a*) Inventory		80,000
(*b*) Trade Receivables		1,20,000

(*c*) Cash and Bank Balance	3	60,000
(*d*) Other Current Assets	4	5,000
TOTAL		9,85,000

Notes :

		₹
(1) Equity Share Capital :		
4,000 Equity Shares of ₹100 each		4,00,000
Preference Share Capital :		
3,000, 5% Preference Shares of ₹100 each		3,00,000
		7,00,000
(2) Reserve & Surplus :		
Reserves	5,000	
Profit & Loss Balance	1,06,000	1,11,000
(3) Cash and Bank Balance :		
Cash Balance	15,000	
Bank Balance	45,000	60,000
(4) Other Current Assets :		
Prepaid Expenses		5,000

SOLUTION :

(*i*) **Acid Test Ratio** $= \dfrac{\text{Liquid Assets}}{\text{Current Liabilities}}$

Liquid Assets = Trade Receivables + Cash Balance + Bank Balance

= 1,20,000 + 15,000 + 45,000 = 1,80,000

Current Liabilities = Trade Payables

= 24,000

Acid Test Ratio $= \dfrac{1{,}80{,}000}{24{,}000} = 7.5 : 1$

(*ii*) **Gross Profit Ratio** $= \dfrac{\text{Gross Profit}}{\text{Net Revenue from Operations}} \times 100$

$= \dfrac{2{,}80{,}000}{5{,}00{,}000} \times 100 = 56\%$

(*iii*) **Inventory Turnover Ratio** $= \dfrac{\text{Cost of Revenue from Operations}}{\text{Average Inventory}}$

Cost of Revenue from Operations = Net Revenue from Operations – Gross Profit

= 5,00,000 – 2,80,000 = 2,20,000

Average Inventory $= \dfrac{\text{Opening Inventory} + \text{Closing Inventory}}{2}$

$= \dfrac{50{,}000 + 80{,}000}{2} = 65{,}000$

Inventory Turnover Ratio $= \dfrac{2{,}20{,}000}{65{,}000} = 3.38$ times

(*iv*) Debt Equity Ratio = $\frac{\text{Long Term Debts}}{\text{Shareholder's Funds}}$

Shareholder's Funds = Preference Share Capital + Equity Share Capital + Reserves + Profit & Loss Balance

= 3,00,000 + 4,00,000 + 5,000 + 1,06,000

= 8,11,000

Debt Equity Ratio = $\frac{1,50,000}{8,11,000} = .18 : 1$

ILLUSTRATION 113.

From the following information, calculate any two of the following ratios :

(*i*) Liquid Ratio
(*ii*) Debt-Equity Ratio
(*iii*) Working Capital Trunover Ratio

Information :

	₹
Net Revenue from Operations	3,00,000
Gross Profit	1,00,000
Total Current Assets	2,00,000
Closing Inventory	20,000
Prepaid Insurance	4,000
Total Current Liabilities	1,20,000
Share Capital	3,50,000
Reserves & Surplus	33,000
Non Current Assets	4,30,000

SOLUTION :

(*i*) Liquid Ratio = $\frac{\text{Quick Assets}}{\text{Current Liabilities}}$

Quick Assets = Current Assets – Closing Inventory – Prepaid Insurance

= ₹2,00,000 – ₹20,000 – ₹4,000 = ₹1,76,000

Liquid Ratio = $\frac{₹\ 1,76,000}{₹\ 1,20,000} = 1.47 : 1$

(*ii*) Debt-Equity Ratio = $\frac{\text{Long term Debts}}{\text{Shareholder's Funds}}$

Long term Debts = Total Current Assets + Non Current Assets – Current Liabilities – Share Capital – Reserve and Surplus

= 2,00,000 + 4,30,000 – 1,20,000 – 3,50,000 – 33,000 = ₹1,27,000

Shareholder's Funds = Share Capital + Reserves and Surplus

= 3,50,000 + 33,000 = 3,83,000

Debt-Equity Ratio = $\frac{₹\ 1,27,000}{₹\ 3,83,000} = .33 : 1$

(*iii*) Working Capital Turnover Ratio $= \dfrac{\text{Net Revenue from Operations}}{\text{Working Capital}}$

Working Capital = Current Assets – Current Liabilities

= ₹2,00,000 – ₹1,20,000 = ₹80,000

Working Capital Turnover Ratio $= \dfrac{₹\ 3{,}00{,}000}{₹\ 80{,}000} = 3.75$ Times

ILLUSTRATION 114.

On the basis of the following information, calculate :

(*i*) Debt-Equity Ratio and

(*ii*) Working Capital Turnover Ratio

Information :	₹
Net Revenue from Operations	60,00,000
Cost of Revenue from Operations	45,00,000
Other Current Assets	11,00,000
Current Liabilities	4,00,000
Paid up share capital	6,00,000
6% Debentures	3,00,000
9% Loan	1,00,000
Debenture Redemption Reserve	2,00,000
Closing Inventory	1,00,000

SOLUTION :

(*i*) Debt-Equity Ratio $= \dfrac{\text{Debt}}{\text{Equity}}$

Debt = 6% Debentures + 9% Loan

= ₹3,00,000 + ₹1,00,000 = ₹4,00,000

Equity = Paid up Share Capital + Debenture Redemption Reserve

= ₹6,00,000 + ₹2,00,000 = ₹8,00,000

Debt-Equity Ratio $= \dfrac{4{,}00{,}000}{8{,}00{,}000} = 0.5 : 1$

(*ii*) Working Capital Turnover Ratio $= \dfrac{\text{Net Revenue from Operations}}{\text{Working Capital}}$

Working Capital = Other Current Assets + Closing Inventory – Current Liabilities

= ₹11,00,000 + ₹1,00,000 – ₹4,00,000

= ₹8,00,000

Working Capital Turnover Ratio $= \dfrac{₹60{,}00{,}000}{₹8{,}00{,}000} = 7.5$ times

ILLUSTRATION 115.

From the following information, calculate (upto two decimal places) :

(*i*) Liquid Ratio

(*ii*) Current Ratio

(*iii*) Proprietary Ratio
(*iv*) Working Capital Turnover Ratio
(*v*) Gross Profit Ratio
(*vi*) Operating Ratio
(*vii*) Net Profit Ratio

	₹
Cost of Revenue from Operations	6,00,000
Operating Expenses	50,000
Gross Revenue from Operations	8,00,000
Revenue from Operations Returns	10,000
Total Current Assets	3,00,000
Total Current Liabilities	1,00,000
Total Assets	7,00,000
Closing Inventory	30,000
Prepaid Insurance	5,000
Share Capital	5,60,000
Reserves and Surplus	34,000

(I.S.C. 2012)

SOLUTION :

(*i*) Liquid Ratio $= \dfrac{\text{Liquid Assets}}{\text{Current Liabilities}}$

Liquid Assets = Current Assets – Closing Inventory – Prepaid Insurance

= ₹3,00,000 – ₹30,000 – ₹5,000 = ₹2,65,000

Liquid Ratio $= \dfrac{₹\ 2{,}65{,}000}{₹\ 1{,}00{,}000} = 2.65 : 1$

(*ii*) Current Ratio $= \dfrac{\text{Current Assets}}{\text{Current Liabilities}}$

$= \dfrac{₹\ 3{,}00{,}000}{₹\ 1{,}00{,}000} = 3 : 1$

(*iii*) Proprietary Ratio $= \dfrac{\text{Shareholder's Funds}}{\text{Total Assets}} \times 100$

Shareholder's Funds = Share Capital + Reserves & Surplus

= 5,60,000 + 34,000 = 5,94,000

Proprietary Ratio $= \dfrac{5{,}94{,}000}{7{,}00{,}000} \times 100 = 84.86\%$

(*iv*) Working Capital Turnover Ratio $= \dfrac{\text{Net Revenue from Operations}}{\text{Working Capital}}$

Net Revenue from Operations = Gross Revenue from Operations – Revenue from Operations Returns

= 8,00,000 – 10,000 = 7,90,000

Working Capital = Current Assets – Current Liabilities

= 3,00,000 – 1,00,000 = 2,00,000

$$\text{Working Capital Turnover Ratio} = \frac{7{,}90{,}000}{2{,}00{,}000} = 3.95 \text{ Times}$$

(*v*) Gross Profit Ratio

$$= \frac{\text{Gross Profit}}{\text{Net Revenue from Operations}} \times 100$$

Gross Profit = Net Revenue from Operations – Cost of Revenue from Operations

= 7,90,000 – 6,00,000 = 1,90,000

$$\text{Gross Profit Ratio} = \frac{1{,}90{,}000}{7{,}90{,}000} \times 100 = 24.05\%$$

(*vi*) Operating Ratio

$$= \frac{\text{Cost of Revenue from Operations} + \text{Operating Exp.}}{\text{Net Revenue from Operations}} \times 100$$

$$= \frac{6{,}00{,}000 + 50{,}000}{7{,}90{,}000} \times 100 = 82.28\%$$

(*vii*) Net Profit Ratio

$$= \frac{\text{Net Profit}}{\text{Net Revenue from Operations}} \times 100$$

Net Profit = Gross Profit – Operating Exp.

= 1,90,000 – 50,000 = 1,40,000

$$\text{Net Profit Ratio} = \frac{1{,}40{,}000}{7{,}90{,}000} \times 100 = 17.72\%$$

ILLUSTRATION 116.

From the following Statement of Profit and Loss of Dixon Ltd. for the year 2014-15, calculate (up to two decimal places) :

(*i*) Trade Receivables Turnover Ratio

(*ii*) Inventory Turnover Ratio

(*iii*) Net Profit Ratio

(*iv*) Operating Profit Ratio

Statement of Profit and Loss of Dixon Ltd.
for the year ending 31st March, 2015

Particulars	*Note No.*	
		₹
Revenue from Operations		2,00,000
Other income (Rent received)		10,000
Total Revenue		2,10,000
Expenses		
Purchases		55,000
Change in Inventories	1	3,000
Employee Benefit Expenses	2	5,000

Depreciation		2,000
Other Expenses	3	5,000
Total Expenses		70,000
Profit Before Tax		1,40,000
Less : Tax		(56,000)
Profit after Tax		84,000

Notes to Accounts :

Particulars	*31.03.2015*
	₹
1. **Change in Inventories :**	
Opening Inventory	6,000
Closing Inventory	(3,000)
	3,000
2. **Employee Benefit Expenses :**	
Wages	2,000
Salaries	3,000
	5,000
3. **Other Expenses :**	
Carriage Inward	2,000
Carriage Outward	3,000
	5,000

Additional Information :

	₹
Debtors (as on 31st March, 2015)	7,000
Bills Receivable (as on 31st March, 2015)	5,000
Cash Revenue from operations	50,000

(ISC 2016)

SOLUTION :

(*i*) **Trade Receivables Turnover Ratio** $= \dfrac{\text{Credit Revenue from Operations}}{\text{Average Trade Receivables}}$

Credit Revenue from Operations $= ₹2,00,000 - ₹50,000 = ₹1,50,000$

Average Trade Receivables $= \text{Debtors} + \text{B/R} = ₹7,000 + ₹5,000$

$= ₹12,000$

Trade Receivables Turnover Ratio $= \dfrac{₹1,50,000}{₹12,000} = 12.5$ times

(*ii*) **Inventory Turnover Ratio** $= \dfrac{\text{Cost of Revenue from Operations}}{\text{Average Inventory}}$

Cost of Revenue from Operations $= \text{Purchases} + \text{Change in Inventory}$

$+ \text{Wages} + \text{Carriage Inward}$

$= ₹55,000 + ₹3,000 + ₹2,000 + ₹2,000$

$= ₹62,000$

Average Inventory $= \dfrac{\text{Opening Inventory} + \text{Closing Inventory}}{2}$

$= \dfrac{6{,}000 + 3{,}000}{2} = ₹4{,}500$

Inventory Turnover Ratio $= \dfrac{₹62{,}000}{₹4{,}500} = 13.78$ times

(*iii*) Net Profit Ratio $= \dfrac{\text{Net Profit}}{\text{Revenue from Operations}} \times 100$

$= \dfrac{₹84{,}000}{₹2{,}00{,}000} \times 100 = 42\%$

(*iv*) Operating Profit Ratio $= \dfrac{\text{Operating Profit}}{\text{Revenue from Operations}} \times 100$

Operating Profit = Net Profit + Non operating exp. – Non operating inc

= ₹84,000 + ₹56,000 – ₹10,000 = ₹1,30,000

Operating Profit Ratio $= \dfrac{₹1{,}30{,}000}{₹2{,}00{,}000} \times 100 = 65\%$

ILLUSTRATION 117.

From the following information calculate (up to two decimal places) :

(1) Trade Receivables Turnover Ratio

(2) Operating Profit Ratio

(3) Net Profit Ratio

	₹
Cash Revenue from Operations	1,00,000
Net Purchases	2,97,000
Credit Revenue from Operations	3,00,000
Closing Debtors	80,000
Closing Bills Receivables	60,000
Carriage Inward	3,000
Finance Cost	5,000
Administrative Expenses	40,000
Profit on sale of fixed asset	10,000
Discount Received	7,000

(I.S.C. Sample Paper, 2017

SOLUTION :

(1) **Trade Receivables Turnover Ratio** $= \dfrac{\text{Credit Revenue from Operations}}{\text{Average Trade Receivables}}$

Average Trade Receivables = Closing Debtors + Closing Bills Receivables

= ₹80,000 + ₹60,0000 = ₹1,40,000

Trade Receivables Turnover Ratio $= ₹\dfrac{3{,}00{,}000}{1{,}40{,}000} = 2.14$ times

(2) Operating Profit Ratio $= \dfrac{\text{Operating Profit}}{\text{Revenue from Operations}} \times 100$

(*i*) Revenue from Operations = Cash Revenue from Operations + Credit Revenue from Operations

= ₹1,00,000 + ₹3,00,000 = ₹4,00,000

(*ii*) Operating Profit = Revenue from Operations – Net Purchases – Carriage Inward – Administrative Exp. + Discount received

= ₹4,00,000 – ₹2,97,000 – ₹3,000 – ₹40,000 + ₹7,000

= ₹67,000

Operating Profit Ratio $= \dfrac{67{,}000}{4{,}00{,}000} \times 100 = 16.75\%$

(3) Net Profit Ratio $= \dfrac{\text{Net Profit}}{\text{Revenue from Operations}} \times 100$

Net Profit = Operating Profit – Non Operating Expenses + Net Operating Incomes

= Operating Profit – Finance Cost + Profit on Sale of Fixed Asset

= ₹67,000 – ₹5,000 + ₹10,000

= ₹72,000

Net Profit Ratio $= \dfrac{72{,}000}{4{,}00{,}000} \times 100 = 18\%$

ILLUSTRATION 118.

From the information given below, calculate (upto two decimal places) :

(*i*) Operating Ratio.

(*ii*) Quick Ratio.

(*iii*) Debt to Equity Ratio.

(*iv*) Proprietary Ratio.

(*v*) Working Capital Turnover Ratio.

Particulars	₹
Net revenue from operations	12,00,000
Cost of revenue from operations	9,00,000
Operating expenses	15,000
Inventory	20,000
Other Current Assets	2,00,000
Current Liabilities	75,000
Paid up Share Capital	4,00,000
Statement of Profit and Loss (Dr.)	47,500
Total Debt	2,50,000

(*I.S.C. 2017*)

SOLUTION :

(*i*) Operating Ratio : $= \dfrac{\text{Cost of Revenue from Operations + Operating Exp.}}{\text{Revenue from Operations}} \times 100$

$$= \frac{9{,}00{,}000 + 15{,}000}{12{,}00{,}000} \times 100 = 76.25\%$$

(*ii*) Quick Ratio : $= \dfrac{\text{Quick Assets}}{\text{Current Liabilities}}$

$$= \frac{2{,}00{,}000}{75{,}000} = 2.67 : 1$$

(*iii*) Debt to Equity Ratio $= \dfrac{\text{Long Term Debts}}{\text{Shareholder's Funds}}$

Long Term Debts = Total Debt – Current Liabilities

= ₹2,50,000 – ₹75,000 = ₹1,75,000

Shareholder's Funds = Paid up Share Capital – Dr. Bal. of Profit & Loss

= ₹4,00,000 – ₹47,500 = ₹3,52,500

Debt to Equity Ratio $= \dfrac{1{,}75{,}000}{3{,}52{,}500} = 0.496 : 1$

(*iv*) Proprietary Ratio $= \dfrac{\text{Shareholder's Funds}}{\text{Total Assets}}$

Total Assets = Shareholder's Funds + Total Debt

= ₹3,52,500 + ₹2,50,000 = ₹6,02,500

Proprietary Ratio $= \dfrac{3{,}52{,}500}{6{,}02{,}500} = 0.585 : 1$

(*v*) Working Capital Turnover Ratio $= \dfrac{\text{Revenue from Operations}}{\text{Working Capital}}$

Working Capital = Inventory + Other Current Assets – Current Liabilities

= ₹20,000 + ₹2,00,000 – ₹75,000 = ₹1,45,000

Working Capital Turnover Ratio $= \dfrac{12{,}00{,}000}{1{,}45{,}000} = 8.28$ times.

LLUSTRATION 119.

From the following information calculate the Return on Investment :

Net Profit (after Tax) Ratio	20%
Tax Rate	40%
	₹
Revenue from Operations	12,00,000
Net Fixed Assets	7,00,000
Non-Current Investments (Trade)	1,00,000

Non-Current Investments (Non-Trade)	50,000
Current Assets	1,80,000
Total Debt	5,00,000
10% Debentures	4,00,000
Trade Payables	50,000

(I.S.C. Specimen Question Paper, 2018)

SOLUTION :

Return on Investment $= \dfrac{\text{Net Profit before Interest \& Tax}}{\text{Capital Employed}} \times 100$

Net Profit after Interest & Tax $=$ 20% of Revenue from Operations

$=$ 20% of ₹12,00,000 = ₹2,40,000

	₹
Net Profit After Interest & Tax	2,40,000
Tax Rate 40%	
Net Profit before Tax $2{,}40{,}000 \times \dfrac{100}{60}$ $=$	4,00,000
Add : Interest : 10% on 4,00,000	40,000
Net Profit before Interest & Tax	4,40,000

Capital Employed $=$ Net Fixed Assets + Trade Investments + Working Capital (*i.e.*, Current Assets – Trade Payables)

$=$ ₹7,00,000 + ₹1,00,000 + ₹1,30,000 (*i.e.*, ₹1,80,000 – ₹50,000)

$=$ ₹9,30,000

Return on Investment $= \dfrac{4{,}40{,}000}{9{,}30{,}000} \times 100 = 47.31\%$

ILLUSTRATION 120.

From the following information calculate the following ratios (up to two decimal places)

(*i*) Earning Per Share

(*ii*) Price Earning Ratio

(*iii*) Return on Investments

(*iv*) Working Capital Turnover Ratio

Particulars	₹
Net profit after Interest and Tax	2,40,000
Tax	1,60,000
Net Fixed Assets	10,00,000
Non-current Investments (Non-Trade)	1,00,000
Equity Share Capital (face value ₹10 per share)	5,00,000
15% Preference Share Capital	1,00,000

Reserves and Surplus (including surplus of the year under consideration)	2,00,000
10% Debentures	4,00,000
Revenue from Operations	10,00,000
Working Capital	1,00,000

Note : The market value of an equity share is ₹40. *(I.S.C. 2018)*

SOLUTION :

(*i*) Earning per share $= \dfrac{\text{Net Profit after Tax and Preference Dividend}}{\text{Number of Equity Shares}}$

$= \dfrac{2,40,000 - 15,000}{50,000} = \dfrac{2,25,000}{50,000} = ₹4.5$

(*ii*) Price Earning Ratio $= \dfrac{\text{Market Value of an Equity Share}}{\text{Earning per Share}}$

$= \dfrac{40}{4.5} = 8.89 \text{ times}$

(*iii*) Return on Investments $= \dfrac{\text{Net Profit before Interest and Tax}}{\text{Capital Employed}} \times 100$

$= \dfrac{2,40,000 + 1,60,000 + 40,000}{11,00,000} \times 100$

$= \dfrac{4,40,000}{11,00,000} \times 100 = 40\%$

Note : Capital Employed = Fixed Assets + Working Capital
₹10,00,000 + ₹1,00,000 = ₹11,00,000

OR

Capital Employed = Equity Capital + Pref. Capital + Reserve & Surplus + Debentures – Non Current Investments
= ₹5,00,000 + ₹1,00,000 + ₹2,00,000 + ₹4,00,000 – ₹1,00,000
= ₹11,00,000

(*iv*) Working Capital Turnover Ratio $= \dfrac{\text{Revenue from Operations}}{\text{Working Capital}}$

$= \dfrac{10,00,000}{1,00,000} = 10 \text{ times}$

LLUSTRATION 121.

From the following Statement of Profit & Loss of Gama Ltd. for the year 2017-18, alculate (up-to two decimal places) :

(*i*) Net Profit Ratio

(*ii*) Operating Profit Ratio

(*iii*) Current Ratio, and

(*iv*) Quick Ratio

STATEMENT OF PROFIT AND LOSS OF GAMA LTD.
for the year ending 31st March, 2018

Particulars	*Note No.*	₹
Revenue from Operations		3,00,000
Other Income (Dividend Received)		40,000
Total Revenue		3,40,000
Expenses :		
Purchases		1,80,000
Change in Inventories	1	(4,000)
Employee Benefit Expenses (Salaries)		10,000
Depreciation and Amortization (Depreciation of Fixed Assets)		28,000
Other Expenses	2	6,000
Total Expenses		2,20,000
Profit before Tax		1,20,000
Less : Provision for Tax		(48,000)
Profit after Tax		72,000

Notes to Accounts :

Particulars	₹
1. Change in Inventories :	
Opening Inventory	8,000
Closing Inventory	12,000
	(4,000)
2. Other Expenses :	
Carriage Outward	4,000
Rent	2,000
	6,000

Additional Information :

Total Current Liabilities as on 31st March, 2018	₹50,000
Current Assets (other than inventory) as on 31st March, 2018	₹70,000

(I.S.C. 2019)

SOLUTION :

(*i*) Net Profit Ratio $= \dfrac{\text{Net Profit}}{\text{Revenue from Operations}} \times 100$

$= \dfrac{72,000}{3,00,000} \times 100 = 24\%$

(*ii*) Operating Profit Ratio $= \dfrac{\text{Operating Profit}}{\text{Revenue from Operations}} \times 100$

Operating Profit $=$ Gross Profit – Operating Expenses

Gross Profit = Revenue from Operations – Cost of Revenue from Operations

= Revenue from Operations – (Opening Inventory + Purchases – Closing Inventory)

= 3,00,000 – (8,000 + 1,80,000 – 12,000)

= 3,00,000 – 1,76,000 = 1,24,000

Operating Expenses = Employee Benefit Exp. + Depreciation + Other Exp.

= ₹10,000 + ₹28,000 + ₹6,000 = ₹44,000

Operating Profit = 1,24,000 – 44,000 = 80,000

Operating Profit Ratio = $\frac{80,000}{3,00,000} \times 100 = 26.67\%$

Alternatively : Operating Profit may also be calculated as follows :

Operating Profit = Net Profit + Non Operating Exp. – Non Operating Income

= 72,000 + 48,000 (Prov. for Tax) – 40,000 (Dividend Recd.) = 80,000

(*iii*) Current Ratio = $\frac{\text{Current Assets}}{\text{Current Liabilities}}$

Current Assets = Closing inventory + Other Current Assets

= 12,000 + 70,000 = 82,000

= $\frac{82,000}{50,000} = 1.64 : 1$

(*iv*) Quick Ratio = $\frac{\text{Quick Assets}}{\text{Current Liabilities}}$

= $\frac{70,000}{50,000} = 1.4 : 1$

ILLUSTRATION 122.

From the following information, calculate the following ratios (up to two decimal places) :

(*i*) Debt to Total Assets Ratio
(*ii*) Proprietary Ratio
(*iii*) Inventory Turnover Ratio

Particulars	₹
Current Assets (including inventory of ₹2,00,000)	10,00,000
Shareholders' Funds	14,40,000
Non-Current Liabilities (10% Long-term Bank Loan)	8,00,000
Current Liabilities	5,00,000
Revenue from Operations	15,00,000
Gross Profit	6,00,000

(I.S.C. 2020, Modified)

SOLUTION :

(*i*) Debt to Total Assets Ratio = $\frac{\text{Debt}}{\text{Total Assets}}$

Debt = 10% Long-term Bank Loan i.e. ₹8,00,000

Total Assets = Shareholder's Funds + Total Debts (*i.e.* Non-Current Liabilities + Current Liabilities)

= ₹14,40,000 + ₹8,00,000 + ₹5,00,000 = ₹27,40,000

Debt to Total Assets Ratio $= \frac{8,00,000}{27,40,000} = 0.29 : 1$

(*ii*) Proprietary Ratio $= \frac{\text{Equity (Shareholder's Funds)}}{\text{Total Assets}}$

$= \frac{14,40,000}{27,40,000} = 0.53 : 1$

(*iii*) Inventory Turnover Ratio $= \frac{\text{Cost of Revenue from Operations}}{\text{Average Inventory}}$

Cost of Revenue from Operations = Revenue from Operations – Gross Profit

= ₹15,00,000 – ₹6,00,000

= ₹9,00,000

Inventory Turnover Ratio $= \frac{9,00,000}{2,00,000} = 4.5$ times

SHORT ANSWER QUESTIONS

(Questions Carrying 2 Marks)

Q. 1. What is meant by Ratio?

[**Ans.** Relationship between two figures expressed in arithmetical terms is called a ratio. A ratio is simply one number expressed in terms of another. It can be expressed in the form of fractions, rate or percentages.]

Q. 2. What is 'Ratio Analysis'?

[**Ans.** According to Myers, ratio analysis is a study of relationship among various items or group of items in financial statements.]

Q. 3. Give two Objectives of Ratio Analysis.

[**Ans.** (*i*) To locate the weak spots of business which need more attention.

(*ii*) To provide deeper analysis of the profitability and financial position of the business.]

Q. 4. Give two uses of Ratio Analysis.

[**Ans.** (*i*) Helpful in judging the profitability of the business.

(*ii*) Helpful in judging the liquidity of the business.]

Q. 5. Give two limitations of ratio analysis.

[**Ans.** (*i*) Ratio analysis becomes less effective due to price level changes.

(*ii*) It is effected by personal bias of the analyst.]

Q. 6. How does the quality of ratio analysis depend upon the accuracy of its financial statements? *(I.S.C. 2014)*

[**Ans.** Ratios are calculated on the basis of data given in profit and loss statement and balance sheet. Hence, they will be only as correct as the accounting data on which they are based. For example, if the closing inventory is over-valued, not only the profitability will be overstated but the financial position will also appear to be better.]

Q. 7. "Accounting ratios ignore qualitative factors and are also not comparable if different firms follow different accounting policies." Comment.

[**Ans.** Ratio analysis is the quantitative measurement of the performance of a business. It ignores the qualitative factors. For example, while conducting the credit analysis of a customer seeking credit, he may deserve the credit to be granted on the basis of financial statements submitted by him but in reality his character (*i.e.*, his intention to pay) and credit worthiness may be doubtful. Further, different firms adopt different accounting policies for inventory valuation, estimating the working life of an asset and in selecting the method of depreciation (*e.g.*, Straight Line or Written Down). Hence, the adoption of different policies by different firms will give different data which will give misleading results if compared.]

Q. 8. Mention two ratios in which both the figures are from Statement of Profit and Loss.

[**Ans.** (*i*) G.P. Ratio and (*ii*) Operating Ratio.]

Q. 9. Mention two ratios in which both the figures are from Balance Sheet.

Or

Mention two Balance Sheet Ratios. *(I.S.C. 2008)*

[**Ans.** (*i*) Current Ratio and (*ii*) Quick Ratio.]

Q. 10. Mention two ratios in which one figure is from Profit and Loss Account and one from Balance Sheet.

[**Ans.** (*i*) Working Capital turnover Ratio and (*ii*) Trade Receivables Turnover Ratio.]

LIQUIDITY RATIOS :

Q. 11. How will you assess the liquidity or short-term financial position of a business?

[**Ans.** Short-term financial position of the business is assessed by calculating current ratio and liquid ratio.]

Q. 12. State the objective of calculating Liquidity Ratios. *(I.S.C. 2020)*

[**Ans.** Liquidity ratios (i.e. Current Ratio and Quick Ratio) show the short-term olvency of the business i.e. the capacity or ability of a firm to meet its short-term abilities as and when they become due.]

Q. 13. What is Current Ratio?

[**Ans.** Current Ratio explains the relationship between Current Assets and Current iabilities of an enterprise. The formula for calculating the ratio is :

$$\text{Current Ratio} = \frac{\text{Current Assets}}{\text{Current Liabilities}}]$$

Q. 14. What is meant by Current Assets?

[**Ans.** Current Assets are those assets which are expected to be converted into Cash or sold or consumed in the production of goods or rendering the service normally within one year's time. These include Cash, short-term investments, trade receivables, inventory, prepaid expenses etc.]

Q. 15. What is meant by Current Liabilities?

[**Ans.** Current Liabilities are those liabilities which fall due for payment normally within one year's time. These include Bank Overdraft, Trade Payables, Outstanding expenses, provision for taxation, proposed dividends etc.]

Q. 16. Why is the Bank Overdraft included in Current Liability?

[**Ans.** Bank Overdraft facility may be withdrawn by the bank at any time. Hence, as per prudence or conservative concept of accounting, bank overdraft is treated as a current liability.]

Q. 17. What is an ideal current ratio and quick ratio?

[**Ans.** An ideal current ratio is 2 : 1 and ideal quick ratio is 1 : 1.]

Q. 18. Assuming that the current ratio of a company is 0.7 : 1, mention whether this ratio would *increase, decrease* or *not change* after the following transactions :

(*i*) Payment of ₹15,000 made to a creditor.

(*ii*) Purchase of inventory worth ₹1,00,000 on credit. *(I.S.C. 2020)*

[**Ans.** (*i*) Decrease (*ii*) Increase]

Q. 19. Current ratio of Reliance Textiles Ltd. is 1.5 at present. In future it wants to improve this ratio to 2. Suggest any two accounting transactions for improving the current ratio.

[**Ans.** (*i*) Payment of current liabilities, (*ii*) Issue of share capital or raising long-term loan.]

Q. 20. What is Liquid Ratio?

[**Ans.** It is a more rigorous test of liquidity than the current ratio. It is calculated by dividing liquid assets by current liabilities.

$$\text{Liquid Ratio} = \frac{\text{Liquid Assets}}{\text{Current Liabilities}}]$$

Q. 21. What are liquid assets?

[**Ans.** 'Liquid Assets' means those assets which will yield cash very shortly. Current assets except inventory and prepaid expenses are included in liquid assets.]

Q. 22. When calculating the Acid Test Ratio, name two items that are excluded from current assets. *(I.S.C. 2008)*

[**Ans.** Inventory and Prepaid expenses.]

Q. 23. What are the other names of liquid ratio?

[**Ans.** Quick ratio and acid test ratio.]

Q. 24. Why liquid ratio is considered more dependable than current ratio?

[**Ans.** Liquid ratio is more dependable because it includes only those assets which can be easily and readily converted into cash. Inventory is not included in liquid assets because it may take a lot of time before it is converted into cash.]

Q. 25. Give one point of distinction between Current Ratio and Quick Ratio.

[**Ans.**

Basis of Distinction	*Current Ratio*	*Quick Ratio*
Relationship	It indicates relationship between Current Assets and Current Liabilities.	It indicates relationship between Quick Assets and Current Liabilities.]

Q. 26. Can Current Ratio and Quick Ratio be same at any moment?

[**Ans.** Yes, if there are no prepaid expenses and inventory in the business.]

Q. 27. State one transaction which results in an increase in 'Liquid Ratio' and no change in 'Current Ratio'.

[**Ans.** Sale of Inventory at Cost Price.]

Q. 28. Why inventory is excluded from liquid assets?

[**Ans.** Inventory is excluded from liquid assets because :

(*i*) there is uncertainty whether it will be sold or not and at what price it will be sold;

(*ii*) it will take time before it is converted into trade receivables and cash.]

Q. 29. Why prepaid expenses are considered as Current assets?

[**Ans.** They are treated as Current assets because if the expenditure for such expenses had not been incurred, cash would have to be spent in the near future.]

Q. 30. Why prepaid expenses are not considered as liquid assets?

(ISC Sample Paper 2017)

[**Ans.** Prepaid expenses are not considered as liquid assets because they cannot be converted into cash.]

Q. 31. What will be the impact of 'Cash Paid to Trade Payables' on a Current Ratio of 2 : 1? State the reason.

[**Ans.** Current Ratio will improve because both Current assets and Current liabilities are decreased by the same amount.]

Q. 32. What will be the impact of 'Cash Paid to Trade Payables' on a Current ratio of 1 : 1? State the reason.

[**Ans.** Current ratio will not alter because both Current assets and Current liabilities are decreased by the same amount.]

Q. 33. What will be the impact of 'Cash paid to Trade Payables' on a Current ratio of .8 : 1? State with reason.

[**Ans.** Current ratio will decrease because both Current assets and Current liabilities are decreased by the same amount.]

Q. 34. What will be the impact of 'Cash collected from Trade Receivables' on a Current ratio of 2 : 1? State with reason.

[**Ans.** No effect because neither the Current assets nor the Current liabilities are affected. Only one Current asset is converted into another Current asset.]

Q. 35. What will be the impact of 'Bills Payable given to Creditors' on a liquid ratio of 1 : 1? State with reason.

[**Ans.** Liquid ratio will not alter because neither the liquid assets nor the current liabilities are affected. Only one current liability is converted into another current liability.]

Q. 36. What will be the impact of 'B/R received from debtors' on a Quick Ratio of 1 : 1?

[**Ans.** It will have no effect on the quick ratio because neither the total quick assets nor the total current liabilities are effected. It is merely a conversion of one quick asset into another quick asset.]

Q. 37. Quick ratio of a company is 1.5 : 1. State giving reason whether the ratio will improve, decline or not change on payment of dividend by the company.

[**Ans.** Quick ratio will improve as both the liquid assets and current liabilities will decrease by the same amount.]

Q. 38. The Quick Ratio of a company is 0.8 : 1. State whether the Quick Ratio will improve, decline or will not change in the following cases :

(*i*) Cash collected from Debtors ₹50,000.
(*ii*) Creditors of ₹20,000 paid off. *(I.S.C. 2018)*

[**Ans.** (*i*) No change (*ii*) Decline]

SOLVENCY RATIOS :

Q. 39. What is Debt Equity Ratio?

[**Ans.** This ratio measures the ability of the firm to meet its long-term liabilities. It indicates the funds provided by long-term lenders in comparison to the funds provided by the owners *i.e.*, shareholders :

$$\text{Debt Equity Ratio} = \frac{\text{Debt}}{\text{Equity}} = \frac{\text{Long term Debts}}{\text{Shareholder's Funds}}]$$

Q. 40. What will a higher debt-equity ratio indicate?

[**Ans.** It will indicate a risky financial position from the long-term point of view, as it indicates that a higher proportion of funds invested in the business is provided by long-term lenders.]

Q. 41. What is proprietary ratio? *(ISC Sample Paper, 2017)*

[**Ans.** It captures relationship between equity and total assets. The following is the formula :

$$\text{Proprietary Ratio} = \frac{\text{Equity (Shareholder's Funds)}}{\text{Total Assets}}]$$

Q. 42. What does proprietary ratio indicate?

[**Ans.** It indicates the proportion of total assets financed by shareholder's funds.]

Q. 43. What does a low proprietary ratio indicate?

[**Ans.** It indicates more use of long-term loans in financing total assets of the enterprise.]

Q. 44. State one transaction which results in a decrease in 'Debt-Equity Ratio' and no change in 'Current Ratio'.

[**Ans.** Issue of shares against the purchase of building or Conversion of debentures into shares.]

Q. 45. The debt-equity ratio of a company is 0.8 : 1. State whether the long term loan obtained by the company will increase, decrease or not change the ratio.

[**Ans.** Debt-equity ratio will increase because long-term debts are increased but total equity remain unchanged.]

Q. 46. What will be the impact of 'Issue of shares against the purchase of fixed ssets' on a debt equity ratio of 1 : 1?

[**Ans.** Debt equity ratio will decrease because the Long-term Loans remain nchanged whereas the Shareholder's Funds are increased by the amount of share apital issued.]

Q. 47. What will be impact of 'purchase of a fixed asset on a credit of 3 months' n a debt equity ratio of 1 : 1?

[**Ans.** There will be no effect on debt equity ratio because the long-term loans as ell as the Shareholder's Funds remain unchanged.]

Q. 48. The Debt-Equity Ratio of *X* Ltd. is 1 : 2. What is the effect of conversion of ebentures into preference shares on this ratio?

[**Ans.** Debt-equity ratio will decrease because conversion of debentures into reference shares will reduce the long-term debts but increase the shareholders' nds.]

Q. 49. Assuming that the Debt-Equity Ratio of a company is 2 : 1, state whether is ratio would increase, decrease or not change in the followng cases :

(*a*) Issue of new shares for cash.

(*b*) Repayment of a long-term bank loan. *(I.S.C. 2012)*

[**Ans.** (*a*) Decrease (*b*) Decrease]

Q. 50. The Debt Equity Ratio of a company is 2 : 1. State which of the following ould improve, reduce or not change the ratio :

(*i*) Issue of Equity Shares for the purchase of Plant and Machinery worth ₹4,00,000.

(*ii*) Sale of Furniture (Book value ₹4,00,000) for ₹3,50,000.

(I.S.C. Specimen Question Paper 2018)

[**Ans.** (*i*) Decrease (*ii*) Increase]

Q. 51. What is Debt to Total Assets Ratio?

[**Ans.** It expresses the relationship between long-term loans and total assets. It is lculated as under :

$$\text{Debt to Total Assets Ratio} = \frac{\text{Long Term Debts}}{\text{Total Assets}}]$$

Q. 52. What does Debt to Total Assets Ratio indicate?

[**Ans.** It measures the extent to which long term loans are covered by assets which indicates the margin of safety available to providers of long term loans. A lower debt to total assets ratio implies the use of lower debts in financing the assets which means a larger safety margin for lenders.]

ACTIVITY RATIOS :

Q. 53. What does activity ratio show?

[**Ans.** Activity ratio shows the rapidity with which assets of the business are being utilised.]

Q. 54. Name two important activity ratios.

[**Ans.** Inventory Turnover Ratio and Trade Receivables Turnover Ratio.]

Q. 55. What is Inventory Turnover Ratio?

[**Ans.** It indicates the relationship between the cost of revenue from operations and average inventory. It shows how quickly inventory is rotated into revenue from operations or the number of times the inventory is turned into revenue from operations during the year.

$$\text{Inventory Turnover Ratio} = \frac{\text{Cost of Revenue from Operations}}{\text{Average Inventory}}]$$

Q. 56. What is indicated by High Inventory Turnover Ratio?

[**Ans.** A high inventory turnover ratio indicates that inventory is being rotated into Revenue from Operations more quickly. An improvement in this ratio shows that either the same volume of Revenue from Operations has been maintained with lower investment in inventory or the volume of Revenue from Operations has increased without any increase in inventory.]

Q. 57. What does Trade Receivables Turnover Ratio indicate?

[**Ans.** It indicates the speed with which the amount is collected from trade receivables. It is calculated as follows :

$$\text{Trade Receivables Turnover Ratio} = \frac{\text{Net Credit Revenue from Operations}}{\text{Average Debtors + Average B/R}}]$$

Q. 58. What is the significance of Trade Receivables Turnover Ratio?

[**Ans.** This ratio indicates the speed with which the amount is collected from debtors. For example, if Trade Receivables Turnover Ratio is 5 times, it means that trade receivables are converted into cash 5 times in a year. Higher trade receivables turnover ratio will show prompt payment by trade receivables and lesser chances of bad debts.]

Q. 59. If Trade Receivables Turnover Ratio is more than the norm set for it, what will it indicate?

[**Ans.** A higher trade receivables turnover ratio will indicate that the amount from trade receivables is being collected more quickly.]

Q. 60. What does too low 'Trade Receivables Turnover Ratio' indicate?

[**Ans.** A too low trade receivables turnover ratio will indicate the liberal and inefficient credit and collection policy of the management. It shows that more money is being locked-up in trade receivables which will result in higher bad-debts, increase in cost of collection and also the loss of interest on the money due from Trade receivables.]

Q. 61. What does too high 'Trade Receivables Turnover Ratio' indicate?

[**Ans.** Normally, a high trade receivables turnover ratio indicates the prompt payments by trade receivables but a too high ratio may be the result of restrictive credit and collection policy of the management which may curtail the revenue from operations and hence may adversely affect the profits.]

Q. 62. What is Trade Payables Turnover Ratio? *(I.S.C. 2015)*

[**Ans.** This ratio indicates the speed with which amount is being paid to Trade Payables. It is calculated as follows :

$$\text{Trade Payables Turnover Ratio} = \frac{\text{Net Credit Purchases}}{\text{Average Creditors} + \text{Average B/P}}]$$

Q. 63. What is Working Capital Turnover Ratio?

[**Ans.** It reveals how efficiently working capital has been utilised in making Revenue from Operations. It is calculated as follows :

$$\text{Working Capital Turnover Ratio} = \frac{\text{Net revenue from Operations}}{\text{Working Capital}}]$$

Q. 64. What does a low working capital turnover ratio indicates?

[**Ans.** A low working capital turnover ratio indicates under-utilisation of working capital.]

PROFITABILITY RATIOS :

Q. 65. What is G.P. Ratio? *(I.S.C. 2009)*

[**Ans.** This ratio measures the margin of gross profit available on Revenue from Operations. The formula for calculating this ratio is :

$$\text{Gross Profit Ratio} = \frac{\text{Gross Profit}}{\text{Net Revenue from Operations}} \times 100]$$

Q. 66. What is N.P. ratio? *(I.S.C. 2009)*

[**Ans.** It measures the margin of net profit available on Revenue from Operations. The formula for calculating this ratio is :

$$\text{Net Profit Ratio} = \frac{\text{Net Profit}}{\text{Net Revenue from Operations}} \times 100]$$

Q. 67. How is 'Cost of Revenue from Operations' Calculated? *(I.S.C. 2009)*

Ans. Cost of Revenue from Operations = Opening Inventory + Net Purchases + Direct Expenses – Closing Inventory

OR

Cost of Revenue from Operations = Net Revenue from Operations – Gross Profit.]

Q. 68. What is Operating Profit? How is it calculated?

[**Ans.** Operating profit is the excess of Revenue from Operations over cost of venue from operations plus operating expenses. Thus it is calculated as below :

Operating Profit = Revenue from Operations – Cost of revenue from erations – Operating Expenses.]

Q. 69. What are Operating Expenses?

[**Ans.** Operating Expenses are the expenses related to normal business activities such as administration expenses, selling and distribution expenses, bad-debts, interest on short-term loans etc.]

Q. 70. What are non-operating expenses?

[**Ans.** Non-operating expenses are the expenses which are not related to normal business activities such as loss on sale of fixed assets, loss from fire, interest on long-term loans etc.]

Q. 71. What is the difference between 'Operating Profit' and 'Net Profit'?

[**Ans.** Operating profit is arrived at after deducting only operating expenses from gross profit whereas net profit is arrived at after deducting all operating as well as non-operating expenses from gross profit.]

Q. 72. What is Operating Ratio? How is it calculated?

[**Ans.** It measures the cost of Revenue from Operations plus operating expenses in comparison to Revenue from Operations.

$$\text{Operating Ratio} = \frac{\text{Cost of Revenue from Operations} + \text{Operating Expenses}}{\text{Net Revenue from Operations}} \times 100]$$

Q. 73. What is the significance of Operating Ratio?

[**Ans.** It indicates the extent of Revenue from Operations that is absorbed by the cost of Revenue from Operations and operating expenses. Lower the operating ratio, the better it is, because it will leave higher margin of profit on Revenue from Operations.]

Q. 74. What is meant by 'Operating Cost'?

[**Ans.** Operating cost is the composition of cost of revenue from operations and other operating expenses such as Office and Administrative expenses, selling and distribution expenses, discount allowed, bad-debts, interest on short-term loans etc.]

Q. 75. What items are included in the Shareholder's Fund?

[**Ans.** Shareholder's Funds include Equity Share Capital, Preference Share Capital, Profits, Reserves minus Accumulated losses.]

Q. 76. What items are included in Equity Shareholder's Fund?

[**Ans.** Equity Shareholder's Fund include Equity Share Capital, Profits, Reserves minus Accumulated losses.]

Q. 77. Give the formula for calculating earning per share. *(ISC, 2015)*

Ans. Earning Per Share (E.P.S.)

$$= \frac{\text{Net Profit (after Interest, Tax and Dividend on Preference Shares)}}{\text{Number of Equity Shares}}$$

PRACTICAL QUESTIONS

(Q. Nos. 1 to 110 are strictly in the serial order of Illustrations)

Liquidity Ratios :—

Q. 1. From the following particulars compute the Current Ratio :

	₹
Land & Buildings	5,00,000
Inventory	70,000
Trade Receivables	90,000
Current Investments	35,000
Trade Payables	46,000
Long term Borrowings	50,000
Short term Borrowings	20,000
Provision for Tax	10,000
Outstanding Expenses	4,000
Cash and Bank Balance	5,000

[**Ans.** Current Ratio 2.5 : 1]

Q. 2. Following particulars are given to you :

		₹
Goodwill		1,00,000
Inventories		2,50,000
Trade Receivables	1,35,000	
Less : Provision	5,000	1,30,000
Investments (Short term)		30,000
Expenses paid in Advance		20,000
Cash and Bank Balance		40,000
Accrued Income		10,000
Short term Provision		20,000
Short term Borrowings (Bank Overdraft)		30,000
Trade Payables		95,000
Expenses Payable		5,000

Calculate the Current Ratio and Quick Ratio. What Conclusions do you draw from these ratios?

[**Ans.** Current Ratio 3.2 : 1; Quick Ratio 1.4 : 1; Short term financial position the Company is quite satisfactory.]

Hint—Accrued Income is included in current assets as well as in quick assets.

Q. 3. From the following compute Current Ratio :

	₹
Total Assets	40,00,000
Non Current Assets	22,00,000
Shareholder's Funds :	
Share Capital	24,00,000

Reserve & Surplus	3,00,000
Non Current Liabilities	8,00,000

[Ans. Current Ratio 3.6 : 1]

Q. 4. Calculate Current Ratio from the following information :

	₹		₹
Total Assets	12,00,000	Non Current Investments	1,40,000
Land and Building	6,00,000	Shareholder's Funds	8,50,000
Machinery	1,00,000	Non Current Liabilities	1,10,000

[Ans. Current Ratio 1.5 : 1]

Q. 5 (A). Current Ratio of a Company is 2 : 1. Which of the following suggestions would improve the ratio, which would reduce it and which would not change it ?

I. Purchase of goods on Credit.
II. Purchase of goods for Cash.
III. Sale of goods Costing ₹50,000 for ₹60,000 on Credit.
IV. To sell a fixed asset at a slight loss.
V. To borrow money on a promissory note (B/P).
VI. To give promissory note to a Creditor.

[Ans. (I) Reduce; (II) No Change; (III) Improve; (IV) Improve; (V) Reduce; (VI) No Change.]

Hints—Transaction I results in increase in inventories (Current Assets) and increase in Trade Payables (Current Liabilities).

Transaction II results in increase in inventories (Current Assets) and decrease in Cash (Current Assets).

Transaction III results in increase in trade receivables (Current Assets) by ₹60,000 and decrease in inventories (Current Assets) by ₹50,000.

Transaction IV results in increase in Cash (Current Assets). Current liabilities remain unchanged.

Transaction V results in increase in Cash (Current Assets) and increase in B/P (Current Liabilities).

Transaction VI results in decrease in Creditor (Current Liabilities) and increase in B/P (Current Liabilities).

Q. 5 (B). The current ratio of a company is 2.5 : 1. Which of the following suggestions would improve, reduce and not change it :

(*i*) Payment to trade payables.
(*ii*) Sell machinery for cash.
(*iii*) Sale of inventory at loss on credit.
(*iv*) Cash collected from trade receivables.
(*v*) B/R dishonoured.
(*vi*) Issue of shares.
(*vii*) Issue of shares against the purchase of a building.
(*viii*) Redemption (Repayment) of Debentures.

[Ans. (*i*) Improve; (*ii*) Improve; (*iii*) Reduce (*iv*) No Change; (*v*) No Change; (*vi*) Improve; (*vii*) No Change; (*viii*) Improve]

Hints : Transaction (*i*) results in decrease in cash (Current Assets) and decrease in Trade Payables (Current Liabilities).

Transaction (*ii*) results in increase in cash (Current Assets). There is no change in Current Liabilities.

Transaction (*iii*) results in decrease in inventory (Current Assets) by higher amount and increase in Trade Receivables (Current Assets) by a lower amount.

Transaction (*iv*) results in increase in cash (Current Assets) and decrease in trade receivables (Current Assets).

Transaction (*v*) results in decrease in B/R (Current Assets) and increase in debtors (Current Assets). There is no change in current liabilities.

Transaction (*vi*) results in increase in cash (Current Assets). There is no change in Current Liabilities.

Transaction (*vii*) affects neither Current Assets nor Current Liabilities.

Transaction (*viii*) results in decrease in cash (Current Assets) and decrease in Current Liabilities since redeemable debentures are included in Current Liabilities.

Q. 6. Assuming that the current ratio is 1.5 : 1, state giving reasons, which of the following transactions would (*i*) improve, (*ii*) reduce, (*iii*) not alter the current ratio :

(*i*) Realisation of current assets
(*ii*) Payment of current liabilities
(*iii*) B/R dishonoured
(*iv*) Sale of goods at par
(*v*) Sale of goods at profit
(*vi*) Sale of goods at loss
(*vii*) Purchase of goods for cash
(*viii*) Purchase of goods on credit
(*ix*) Sale of furniture for cash
(*x*) Sale of machinery on a credit of 5 months
(*xi*) Sale of land on long-term deferred payment basis
(*xii*) Purchase of motor car for cash
(*xiii*) Purchase of a building on a credit of 4 months
(*xiv*) Purchase of a plot of land on long-term deferred payment basis.
(*xv*) Repayment of long-term loan which was availed from a bank.
(*xvi*) Issue of shares for Cash.

[Ans. (*i*) Not alter; (*ii*) Improve; (*iii*) Not alter; (*iv*) Not alter; (*v*) Improve; *vi*) Reduce; (*vii*) Not alter; (*viii*) Reduce; (*ix*) Improve; (*x*) Improve; (*xi*) Not alter; *xii*) Reduce; (*xiii*) Reduce; (*xiv*) Not alter; (*xv*) Reduce; (*xvi*) Improve.]

Q. 7. The Current Ratio of a Company is 3 : 1. State giving reasons which of the following suggestions would (*i*) improve; (*ii*) reduce; (*iii*) not change; the Current Ratio :

(*a*) Payment of Trade Payables.
(*b*) Sale of goods costing ₹20,000 for ₹20,000 for Cash.
(*c*) Sale of goods costing ₹20,000 for ₹18,000 on Credit.
(*d*) Sale of goods costing ₹20,000 at a profit of ₹1,000.
(*e*) Purchase of goods on Credit.
(*f*) Purchase of goods for Cash.
(*g*) Purchase of machinery against long-term loan.

[**Ans.** (*a*) Improve; (*b*) No change; (*c*) Reduce; (*d*) Improve; (*e*) Reduce; (*f*) No change; (*g*) No change.]

Q. 8. State giving reason, whether the Current Ratio will improve or decline or will have no effect in each one of the following transactions if Current Ratio is (I) 2.5 : 1, (II) 1 : 1, (III) 0.75 : 1.

1. Paid ₹50,000 to a Creditor.
2. Sale of goods at a loss of 10%.
3. Sale of a fixed asset for ₹1,00,000 (Book Value ₹1,20,000).
4. Payment of outstanding salaries.
5. Received ₹25,000 from a Debtor of ₹30,000 in full settlement of his account
6. Bills payable discharged on maturity
7. Bills Receivable drawn on debtor
8. Purchased goods on credit
9. Issued debentures to the vendors of machinery

[**Ans.** (*i*) If Current Ratio is 2.5 : 1.
Improve : 1, 3, 4, 6; Decline : 2, 5, 8; No effect : 7, 9
(*ii*) If Current Ratio is 1 : 1.
Improve : 3; Decline : 2, 5; No effect : 1, 4, 6, 7, 8, 9
(*iii*) If Current Ratio is 0.75 : 1.
Improve : 3, 8; Decline :1, 2, 4, 5, 6; No effect : 7, 9]

Q. 9. State giving reasons which of the following transactions would Improve; Reduce; or Not change the Quick Ratio if Quick Ratio is (*i*) 1.5 : 1; (*ii*) 1 : 1 or (*iii*) 0.8 : 1

(*a*) Payment of Outstanding Liabilities
(*b*) Debentures of ₹2,00,000 converted into equity shares
(*c*) Purchase of goods on Credit of 2 months.
(*d*) B/R endorsed to a Creditor.
(*e*) Sale of goods Costing ₹50,000 for ₹45,000.
(*f*) B/R drawn on a Debtor.
(*g*) Paid Rent ₹3,000 in advance.
(*h*) Trade receivables included a debtor Sh. Ashok who paid his entire amount due ₹9,700.

[**Ans.** (*i*) If Quick Ratio is 1.5 : 1
(*a*) Improve; (*b*) Not Change; (*c*) Reduce; (*d*) Improve; (*e*) Improve;
(*f*) Not change, (*g*) Reduce; (*h*) Not Change.

(*ii*) If Quick Ratio is 1 : 1
(*a*) Not Change; (*b*) Not Change; (*c*) Reduce; (*d*) Not Change; (*e*) Improve
(*f*) Not Change; (*g*) Reduce; (*h*) Not Change.

(*iii*) If Quick Ratio is 0.8 : 1
(*a*) Reduce; (*b*) Not Change; (*c*) Reduce; (*d*) Reduce; (*e*) Improve;
(*f*) Not Change; (*g*) Reduce; (*h*) Not Change]

Q. 10. Calculate Current Ratio from the following :

Working Capital ₹1,92,000; Long-term Debt ₹80,000 and Total Debt ₹2,00,000.

[**Ans.** 2.6 : 1]

Q. 11. Calculate Current Ratio from the following :

Working Capital ₹4,80,000; Trade Payables ₹2,00,000 and Bank Overdraft ₹40,000.

[**Ans.** 3 : 1]

Q. 12. Calculate Current Ratio and Liquid Ratio from the following :

	₹
Cash and Cash Equivalents	40,000
Trade Receivables	2,70,000
Inventories (Includes Loose Tools ₹30,000)	1,80,000
Prepaid Expenses	20,000
Working Capital	2,80,000

[**Ans.** Current Ratio 2.4 : 1; Liquid Ratio 1.55 : 1.]

Q. 13. Calculate Current Ratio from the following :

Working Capital ₹4,80,000; Current Assets ₹6,00,000; Inventory ₹4,00,000 and Trade Receivables ₹1,50,000.

[**Ans.** 5 : 1]

Q. 14 (A). A firm had current assets of ₹4,10,000. It then paid creditors of ₹50,000. After this payment, the current ratio was 2.4 : 1. Ascertain the amount of Current Liabilities and Working Capital after the payment.

[**Ans.** Current Liabilities ₹1,50,000; Working Capital ₹2,10,000.]

Q. 14 (B). A firm had current assets of ₹7,20,000. It then purchased goods for ₹30,000 on credit. After this purchase, the current ratio was 3 : 1. Ascertain the amount of Current Liabilities and Working Capital after the purchase.

[**Ans.** Current Liabilities ₹2,50,000; Working Capital ₹5,00,000.]

Q. 15 (A). Current Ratio 2 : 1, Quick Ratio 1.5 : 1, Current Liabilities ₹1,60,000. Calculate Current Assets, Quick Assets and Inventories.

[**Ans.** ₹3,20,000, ₹2,40,000, ₹80,000.]

Q. 15 (B). Current Ratio 2.5 : 1, Quick Ratio .8 : 1, Current Assets ₹2,00,000 Calculate Current Liabilities, Quick Assets and Inventory.

[**Ans.** ₹80,000, ₹64,000, ₹1,36,000.]

Q. 15. (C). Working Capital ₹5,40,000; Current Ratio 2.8 : 1; Inventor ₹3,30,000. Calculate Current Assets, Current Liabilities and Quick Ratio.

[**Ans.** ₹8,40,000; ₹3,00,000; 1.7 : 1.]

Q. 16. A business has a Current Ratio of 4 : 1 and a Quick Ratio of 1.2 : 1. If th Working Capital is ₹1,80,000, calculate the total Current Assets and Inventory.

[**Ans.** Current Assets ₹2,40,000; Inventory ₹1,68,000.]

Q. 17. Current Ratio 2.4; Current Assets ₹1,81,10,400; Inventories ₹79,23,300. Calculate the Liquid Ratio.

[**Ans.** Liquid Ratio 1.35.]

Q. 18. Quick Ratio 1.5; Current Assets ₹1,00,000; Current Liabilities ₹40,000. Calculate the value of Inventory.

[**Ans.** ₹40,000.]

Q. 19. A Company's inventory is ₹2,00,000. Total liquid assets are ₹8,00,000 and quick ratio is 2 : 1. Calculate the current ratio.

[**Ans.** Current Ratio 2.5 : 1.]

Q. 20. A firm has Current Ratio of 4.5 : 1 and Quick Ratio of 3 : 1. If its inventory is ₹72,000, find out its total current assets and total current liabilities.

[**Ans.** Current Assets ₹2,16,000; Current Liabilities ₹48,000.]

Q. 21 (A). Current Assets ₹85,000; Inventory ₹22,000; Prepaid Expenses ₹3,000; Working Capital ₹45,000. Calculate Quick Ratio.

[**Ans.** Quick Ratio 1.5 : 1.]

Hints :— (*i*) Quick Assets = Current Assets – Inventory – Prepaid Expenses
(*ii*) Current Liabilities = Current Assets – Working Capital

Q. 21 (B). Quick Assets ₹90,000; Inventory ₹1,08,000; Prepaid Expenses ₹2,000; Working Capital ₹1,50,000. Calculate Current Ratio.

[**Ans.** Current Ratio 4 : 1.]

Hints :— (*i*) Current Assets = Quick Assets + Inventory + Prepaid Exp.
(*ii*) Current Liabilities = Current Assets – Working Capital

Q. 22. The ratio of Current Assets (₹32,00,000) to Current Liabilities (₹20,00,000) is 1.6 : 1. The accountant of the firm is interested in maintaining a Current Ratio of 2 : 1, by paying off a part of the Current Liabilities. Compute the amount of the Current Liabilities that should be paid, so that the Current Ratio at the level 2 : 1 may be maintained.

[**Ans.** Current liabilities to the extent of ₹8,00,000 should be paid to achieve the Current Ratio at the level of 2 : 1]

Q. 23. The ratio of Current Assets (₹5,00,000) to Current Liabilities is 2.5 : 1. The accountant of this firm is interested in maintaining a Current Ratio of 2 : 1 by acquiring some Current Assets on Credit. You are required to suggest him the amount of Current Assets which must be acquired for this purpose.

[**Ans.** Current Assets to the extent of ₹1,00,000 should be acquired on credit to maintain a Current Ratio of 2 : 1.]

Solvency Ratios :—

Q. 24. Calculate the Debt Equity Ratio from the following :—

	₹
Equity Share Capital	3,00,000
Preference Share Capital	50,000
Reserves	1,60,000

Profit & Loss Balance (Accumulated Loss)	(50,000)
Long-term Borrowings	2,00,000
Provision for Employee Benefits	60,000

[**Ans.** Debt Equity Ratio $= \frac{\text{Debt}}{\text{Equity}} = \frac{\text{Long term Debts}}{\text{Shareholder's Funds}} = 0.57:1$]

Hints : (*i*) Shareholder's Funds = Equity Share Capital + Preference Share Capital + Reserves – P & L

(*ii*) Provision for Employee Benefits will be treated as Long term Provision.

Q. 25. From the following, ascertain Debt-Equity Ratio :

	₹
Share Capital	6,00,000
Capital Reserve	3,20,000
General Reserve	60,000
Profit & Loss Balance	1,40,000
8% Debentures	5,00,000
10% Long term Loan	3,40,000
Long term Provision	1,12,000
Current Liabilities	2,20,000
Current Assets	3,10,000

[**Ans.** Debt Equity Ratio = 0.85 : 1]

Q. 26. Calculate Debt Equity Ratio from the following :

	₹
Tangible Fixed Assets	24,50,000
Intangible Fixed Assets	3,00,000
Current Assets	3,34,000
Current Liabilities	84,000
Long term Borrowings	16,00,000
Long term Provisions	1,50,000

[**Ans.** Debt Equity Ratio = 1.4 : 1]

Hint : Shareholder's Funds = Non Current Assets + Working Capital – Non Current Liabilities
= ₹12,50,000

Q. 27. Calculate Debt Equity Ratio from the following :

Total Assets ₹2,30,000; Total Debt ₹1,50,000; Current Liabilities ₹30,000.

[**Ans.** Debt Equity Ratio $= \frac{\text{Long term Debts}}{\text{Shareholder's Funds}} = 1.5:1$]

Q. 28. The debt-equity ratio of a company is 1 : 2. Which of the following suggestions would increase, decrease or not change it?

(*i*) Issue of Equity Shares
(*ii*) Cash Received from Trade Receivables
(*iii*) Sale of Goods on Cash Basis

(*iv*) Repayment of Long term Borrowings
(*v*) Purchased Goods on Credit

[**Ans.** (*i*) Decrease, (*ii*) No Change, (*iii*) No Change, (*iv*) Decrease, (*v*) No Change.]

Q. 29. Compute Debt to Total Assets Ratio from the following information :

	₹		₹
Total Assets	35,00,000	Bills Payables	20,000
Total Debts	32,00,000	Short-term Borrowings	1,00,000
Creditors	2,50,000	Outstanding Expenses	30,000

[**Ans.** Debt to Total Assets Ratio = .8 : 1]

Q. 30. Calculate Debt to Total Assets Ratio from the following information :

	₹		₹
Shareholder's Funds	32,00,000	Total Debts	24,00,000
Reserve and Surplus	12,00,000	Trade Payables	5,60,000
		Bank Overdraft	40,000

[**Ans.** .32 : 1]

Hint. Reserve and Surplus will be ignored since it is already included in Shareholder's Funds.

Q. 31. From the following information, calculate Debt to Total Assets Ratio :

	₹		₹
8% Debentures	30,00,000	Share Capital	20,00,000
Loan from Bank	10,00,000	Reserve and Surplus	5,00,000
Short term Borrowings	8,60,000	Surplus, *i.e.*, Balance in Statement of Profit & Loss	2,20,000

[**Ans.** .54 : 1]

Hint. Surplus *i.e.*, Balance in Statement of Profit & Loss will be ignored since it is already included in Reserve and Surplus.

Q. 32. Total Debt ₹40,00,000; Share Capital ₹15,00,000; Reserve and Surplus ₹8,00,000; Current Liabilities ₹5,00,000; Working Capital ₹7,00,000. Calculate Debt to Total Assets Ratio.

[**Ans.** .56 : 1]

Q. 33. Calculate Debt to Total Assets Ratio from the following :

	₹		₹
Capital Employed	60,00,000	Trade Payables	8,00,000
Share Capital	20,00,000	Outstanding Expenses	40,000
Reserve and Surplus	16,00,000		

[**Ans.** .35 : 1]

Q. 34. Following particulars are extracted from the books of Bharat Rubber Ltd.:

	₹
Share Capital	3,20,000
General Reserve	1,00,000
Profit & Loss Balance	48,000
9% Debentures	1,20,000
Current Liabilities	3,04,000

You are required to work out the following ratios :—

(*i*) Debt-Equity Ratio; (*ii*) Debt to Total Assets Ratio and (*iii*) Proprietary Ratio.

[**Ans.** (*i*) Debt-Equity Ratio $= \dfrac{\text{Long term Debts}}{\text{Shareholder's Funds}} = .26 : 1$

(*ii*) Debt to Total Assets Ratio $= \dfrac{\text{Long term Debts}}{\text{Total Assets}} = .13 : 1$

(*iii*) Proprietary Ratio $= \dfrac{\text{Shareholder's Funds}}{\text{Total Assets}} \times 100 = 52.47\%.$]

Q. 35. Following particulars are given to you :

	₹
Long term Borrowings	7,00,000
Long term Provisions	2,25,000
Non Current Assets	12,00,000
Current Assets	5,40,000
Current Liabilities	1,40,000

Calculate (*i*) Debt Equity Ratio, (*ii*) Debt to Total Assets Ratio and (*iii*) Proprietary Ratio.

[**Ans.** (*i*) 1.37 : 1, (*ii*) .53 : 1, (*iii*) 38.79%]

Q. 36. Calculate proprietary ratio on the basis of following particulars :

	₹
Non Current Assets	5,00,000
Current Assets	3,00,000
Equity Share Capital	0.4 times of total assets
Preference Share Capital	0.25 times of Equity Share Capital
General Reserve	1,50,000
Net Profit before Tax	1,20,000
Tax Rate	25%

[**Ans.** Proprietary Ratio : 0.8 : 1]

Q. 37. From the following, ascertain Debt-Equity Ratio and Proprietary Ratio :—

	₹
Equity Share Capital	20,00,000
General Reserve	10,00,000
Securities Premium	5,00,000

10% Debentures	3,00,000
Loan from Industrial Development Bank of India (I.D.B.I.)	12,00,000
Current Liabilities	10,00,000
Fixed Assets	40,00,000
Current Assets	20,00,000

[**Ans.** (*i*) Debt-Equity Ratio $= \dfrac{\text{Long term Debts}}{\text{Shareholder's Funds}} = .43 : 1$

(*ii*) Proprietary Ratio $= \dfrac{\text{Shareholder's Funds}}{\text{Total Assets}} = \dfrac{35,00,000}{60,00,000} = 58.33\%$]

Q. 38. Calculate the value of Current Assets of *X* Ltd. from the following information :

	₹
Equity Share Capital	25,00,000
6% Preference Share Capital	5,00,000
General Reserve	8,00,000
Profit & Loss Balance	(2,00,000)
Fixed Assets	30,00,000
Proprietary Ratio	0.75 : 1

[**Ans.** Current Assets ₹18,00,000.]

Q. 39. From the following information, calculate interest coverage ratio and give your comments also :

	₹
Net Profit after Interest and Tax	1,20,000
Rate of Income Tax	50%
15% Debentures	1,00,000
12% Mortgage Loan	1,00,000

[**Ans.** Interest Coverage Ratio = 9.89 times.]

Comments : An interest coverage ratio of 6 to 7 times is considered appropriate. As the actual interest coverage ratio of this company is nearly 10 times, it means that the company will be able to pay the interest on long-term loans regularly.

Q. 40. The following particulars are given to you :

	₹
Share Capital	1,00,000
Reserve and Surplus	1,50,000
Current Liabilities	4,00,000
Current Assets	5,50,000
Tangible Fixed Assets	7,00,000
Loans @10%	4,00,000
12% Debentures	2,00,000

Net Profit for the year after interest and tax was ₹96,000. Rate of Income Tax was 50%.

Calculate (*i*) Debt Equity Ratio; (*ii*) Proprietary Ratio; and (*iii*) Interest Coverage Ratio.

Also give your comments.

[**Ans.** (*i*) Debt-Equity Ratio $= \dfrac{\text{Long term Debts}}{\text{Shareholder's Funds}} = 2.4 : 1$

(*ii*) Proprietary Ratio $= \dfrac{\text{Shareholder's Funds}}{\text{Total Assets}} \times 100 = 20\,\%$

(*iii*) Interest Coverage Ratio = 4 times

Comments : (*i*) Debt-Equity Ratio of the Company is not satisfactory because it is more than the acceptable norms of 2 : 1. It shows risky financial position from the long-term point of view.

(*ii*) Proprietary Ratio is only 20% which means that the long-term financial position of the Company is not satisfactory because only 20% of the total assets of the company are funded by equity.

(*iii*) Normally acceptable interest-coverage ratio is 6 or 7 times, whereas the actual ratio for this company is 4. It means that the company may face difficulty in paying the interest on long-term loans regularly in case of fall of profits.

Activity Ratios or Turnover Ratios :—

Q. 41. Calculate inventory turnover ratio from the following :—

	₹
Opening Inventory	92,400
Closing Inventory	67,600
Purchases	2,75,200
Revenue from Operations (Sales)	5,00,000
Revenue from Operations Returns (Sales Return)	20,000

[**Ans.** Inventory Turnover Ratio 3.75 Times.]

Q. 42. Calculate Inventory Turnover Ratio from the following :

	₹
Purchases	3,46,000
Returns Outwards	10,000
Carriage Inwards	15,000
Carriage Outwards	20,000
Wages	25,000
Salaries	40,000
Rent	36,000
Opening Inventory	72,000
Closing Inventory	88,000

[**Ans.** Inventory Turnover Ratio 4.5 times.]

Hint. Carriage Outwards, Salaries and Rent will be ignored while calculating Inventory Turnover Ratio.

Q. 43. Following is the Statement of Profit & Loss of Triveni Ltd. Calculate nventory Turnover Ratio :

STATEMENT OF PROFIT AND LOSS
for the year ended 31st March, 2020

Particulars	*Note No.*	₹
I. Revenue from Operations (Sales)		10,00,000
II. Other Income		50,000
III. Total Revenue (I + II)		10,50,000
IV. Expenses		
Purchase of Stock in Trade		5,36,000
Change in Inventories of Stock in Trade	1	25,000
Employee Benefit Exp.		1,20,000
Finance Costs		30,000
Other Expenses		24,000
Total Expenses		7,35,000
V. Profit before Tax (III – IV)		3,15,000
Less : Income Tax		1,25,000
VI. Profit after Tax		1,90,000

Notes to Accounts :

Particulars	₹
1. **Opening Inventory**	95,000
Less : Closing Inventory	70,000
	25,000

[**Ans.** Inventory Turnover Ratio 6.8 times.]

Q. 44. Calculate Inventory Turnover Ratio and Average Age of Inventory from the following :

STATEMENT OF PROFIT AND LOSS
for the year ended 31st March, 2020

Particulars	*Note No.*	₹
I. Revenue from Operations (Sales)		12,00,000
II. Expenses :		
Purchase of Stock in Trade	1	6,50,000
Change in Inventories of Stock in Trade	2	(30,000)
Employee Benefit Expenses	3	2,40,000
Other Expenses		90,000
Total Expenses		9,50,000
III. Profit before Tax (I – II)		2,50,000

Notes to Accounts :

Particulars	₹
1. **Change in Inventories of Stock in Trade :**	
Opening Inventory	1,25,000
Less : Closing Inventory	1,55,000
	(30,000)
2. **Employee Benefit Expenses :**	
Wages	1,48,000
Salaries	92,000
	2,40,000
3. **Other Expenses :**	
Manufacturing Expenses	72,000
Administration Expenses	10,000
Selling Expenses	8,000
	90,000

[Ans. Inventory Turnover Ratio 6 Times; Average Age of Inventory 61 days]

Hint. Cost of Revenue from Operations = Purchase of Stock in Trade + Change in Inventory + Wages + Manufacturing Exp.

Q. 45. From the following data, calculate 'Inventory Turnover Ratio' when gross profit ratio is given 20% :

	₹
Cash Sales	1,50,000
Credit Sales	2,50,000
Return Inward	25,000
Opening Inventory	25,000
Closing Inventory	35,000

[Ans. 10 Times]

Q. 46. Calculate the (I) Inventory Turnover Ratio and (II) Average Age of Inventory from the following :—

Opening Inventory ₹54,000; Closing Inventory ₹66,000; Revenue from Operations (Sales) ₹5,00,000; Gross profit Ratio 40% on Revenue from Operations.

[Ans. (I) Inventory Turnover Ratio 5 Times and (II) Average Age of Inventory 73 days.]

Q. 47. Calculate Inventory Turnover Ratio from the following :

Opening Inventory ₹42,500; Closing Inventory ₹37,500; Revenue from Operations (Sales) ₹3,00,000; Gross Profit 20% on cost.

[Ans. Inventory Turnover Ratio 6.25 times]

Q. 48. Calculate Inventory Turnover Ratio for the year 2020-21 and 2021-22 from the following information :

	2020-21	2021-22
	₹	₹
Inventory on 31st March	11,00,000	15,00,000
Revenue from Operations	75,00,000	93,60,000
(Gross Profit is 20% on cost of revenue from Operations)		

In the year 2017-18 inventory decreased by ₹3,00,000

[**Ans.** Inventory Trunover Ratio for 2017-18 : 5 times
for 2018-19 : 6 times]

Q. 49. Compute Inventory Turnover Ratio from the following :

	₹
Cost of Revenue from Operations (Cost of Goods Sold)	5,60,000
Purchases	4,40,000
Wages	1,30,000
Carriage Inwards	15,000
Opening Inventory	75,000

[**Ans.** Closing Inventory ₹1,00,000; Inventory Turnover Ratio 6.4 times]

Hint. Wages and Carriage Inwards are direct expenses. Hence, these will be included in cost of revenue from operations.

Q. 50. From the following information, calculate Inventory Turnover Ratio :

Purchases ₹10,00,000; Revenue from Operations (Sales) ₹12,00,000; Direct Expenses ₹48,000; Gross Profit Ratio 15% on Revenue from Operations; Closing Inventory ₹1,64,000.

[**Ans.** Opening Inventory ₹1,36,000; Inventory Turnover Ratio 6.8 times]

Q. 51. From the following information, calculate Inventory Turnover Ratio : Revenue from Operations (Sales) : ₹4,00,000, Average Inventory : ₹55,000. The rate of Gross Loss on Revenue from Operations was 10%. *(C.B.S.E. Sample Paper, 2017)*

[**Ans.** 8 times.]

Q. 52. Calculate Opening Inventory from the following information :

Purchases ₹5,70,000; Freight ₹20,000; Miscellaneous Expenses ₹10,000; Revenue from Operations (Sales) ₹5,00,000; Closing Inventory ₹70,000; Gross Loss 16% on Revenue from Operations.

[**Ans.** Opening Inventory ₹60,000.]

Hints : (*i*) Freight is a component of Direct Expenses. Hence, it will be included in Cost of revenue from Operations.

(*ii*) Miscellaneous Expenses being indirect expenses will not be included in Cost of revenue from Operations.

Q. 53. From the given information, calculate the Inventory Turnover Ratio :

Revenue from Operations (Sales) : ₹2,00,000; GP : 25%; Opening Inventory was 1/4th of the value of Closing Inventory. Closing Inventory was 40% of Revenue from Operations.

[**Ans.** Inventory Turnover Ratio 3 Times.]

Q. 54. Calculate Inventory Turnover Ratio from the following :

	₹
Cash Revenue from Operations (Cash Sales)	6,00,000
Credit Revenue from Operations (Credit Sales)	4,00,000
Gross Profit	25% on Cost

Closing Inventory : 3 times of Opening Inventory
Opening Inventory : 10% of Cost of Revenue from Operations.

[**Ans.** Inventory Turnover Ratio : 5 times.]

Q. 55.

Revenue from Operations (Sales)	₹7,00,000
Gross Profit	₹1,40,000
Inventory Turnover Ratio	7 Times

Find out the value of Closing Inventory, if Closing Inventory is ₹16,000 more than e Opening Inventory.

[**Ans.** Closing Inventory ₹88,000.]

Q. 56.

Cash Revenue from Operations (Cash Sales)	₹1,00,000
Credit Revenue from Operations (Credit Sales)	₹5,00,000
Gross Profit	₹1,20,000
Inventory Turnover Ratio	4 times

Calculate the value of Opening and Closing Inventory in each of the following ternative cases :

Case I If closing inventory was ₹1,00,000 in excess of opening inventory.
Case II If closing inventory was 2 times that in the beginning.
Case III If closing inventory was 2 times more than that in the beginning.
Case IV If closing inventory was 3 times that in the beginning.

[**Ans.**

	Opening Inventory	*Closing Inventory*
	₹	₹
Case I	70,000	1,70,000
Case II	80,000	1,60,000
Case III	60,000	1,80,000
Case IV	60,000	1,80,000]

Q. 57.

Cost of Revenue from Operations	₹ 7,20,000
Inventory Turnover Ratio	4 Times

Find out the value of opening inventory and closing inventory if closing inventory 80% of opening inventory.

[**Ans.** Opening Inventory ₹2,00,000; Closing Inventory ₹1,60,000.]

Q. 58 (A). ₹3,00,000 is the cost of Revenue from Operations (Cost of Goods ld), Inventory turnover 8 times; Inventory at the beginning is 2 times more than the entory at the end. Calculate the values of Opening & Closing Inventory.

[**Ans.** Opening Inventory ₹56,250; Closing Inventory ₹18,750]

Q. 58 (B). ₹1,50,000 is the cost of Revenue from Operations (Cost of Goods Sold), Inventory turnover 8 times; Inventory at the beginning is 1.5 times more than the inventory at the end. Calculate the values of Opening & Closing Inventory.

[**Ans.** Opening Inventory ₹26,786; Closing Inventory ₹10,714]

Q. 59. Average Inventory carried by a trader is ₹60,000; Inventory turnover ratio is 10 times. Goods are sold at a profit of 10% on cost. Find out the profit.

[**Ans.** Profit ₹60,000.]

Q. 60. Determine the amount of Revenue from Operations from the following particulars :—

Opening Inventory	₹40,000
Inventory Turnover Ratio	6 times
Gross Profit 20% of Revenue from Operations (Sales)	

You are informed that closing inventory is two times in comparison to opening inventory.

[**Ans.** Revenue from Operations ₹4,50,000.]

Q. 61. A Company had a liquid ratio of 1.6 : 1 and a current ratio of 2.4 : 1. Its inventory turnover ratio was 5 times. It had total current liabilities of ₹1,50,000.

Find out revenue from operations if the goods are sold at 40% profit on cost.

[**Ans.** Revenue from Operations ₹8,40,000.]

Q. 62. A company's inventory turnover is 5 times. Inventory at the end of the year is ₹4,000 more than inventory at the beginning of the year. Revenue from Operations during the year (all credit) were ₹3,00,000. Rate of Gross Profit is 25% on cost of Revenue from Operations. Current Liabilities at the end of the year were ₹50,000. Quick Ratio is 1 : 1. Calculate :—

(*i*) Cost of Revenue from Operations (Cost of Goods Sold).
(*ii*) Opening inventory.
(*iii*) Closing inventory.
(*iv*) Quick Assets.
(*v*) Current Assets at the end.

[**Ans.** (*i*) ₹2,40,000; (*ii*) ₹46,000; (*iii*) ₹50,000; (*iv*) ₹50,000; (*v*) ₹1,00,000.]

Q. 63. Following information is given to you :

		₹
Revenue from Operations (Sales)		8,00,000
Less : Purchases	5,90,000	
Changes in Inventory (Opening Inventory – Closing Inventory) (44,000 – 60,000)	(–) 16,000	
Direct Expenses	50,000	6,24,000
Gross Profit		1,76,000

BALANCE SHEET
as at 31st March, 2022

Particulars	*Note No.*	₹
I. EQUITY AND LIABILITIES :		
Shareholder's Funds :		
(*a*) Share Capital		4,50,000
(*b*) Reserve & Surplus	1	1,90,000
Non-Current Liabilities :		
Long-term Borrowings	2	2,00,000
Current Liabilities :		
(*a*) Trade Payables		1,50,000
(*b*) Other Current Liabilities	3	10,000
TOTAL		10,00,000
II. ASSETS :		
Non-Current Assets :		
Fixed Assets		7,20,000
Current Assets :		
(*a*) Inventory		60,000
(*b*) Trade Receivables		1,75,000
(*c*) Cash & Bank Balance		25,000
(*d*) Other Current Assets	4	20,000
TOTAL		10,00,000

Notes :		₹
(1)	Reserve & Surplus :	
	General Reserve	1,20,000
	Profit & Loss Balance	70,000
		1,90,000
(2)	Long-term Borrowings :	
	8% Debentures	2,00,000
(3)	Other Current Liabilities :	
	Outstanding Expenses	10,000
(4)	Other Current Assets :	
	Prepaid Expenses	20,000

On the basis of the informations given above, calculate any two of the followin ratios :

(*i*) Liquid Ratio,

(*ii*) Inventory Turnover Ratio, and

(*iii*) Debt Equity Ratio.

[Ans. Liquid Ratio 1.25 : 1; Inventory Turnover Ratio 12 Times; Debt Equit Ratio 0.3125 : 1.]

Q. 64. Calculate Trade Receivables Turnover Ratio from the following :—

	₹
Cash Revenue from Operations (Cash Sales)	3,40,000
Credit Revenue from Operations (Credit Sales)	6,00,000
Opening Trade Receivables	75,000
Closing Trade Receivables	1,25,000

[Ans. Trade Receivables Turnover Ratio 6 Times.]

Q. 65. Calculate Trade Receivables Turnover Ratio and Average Collection Period from the following :—

	₹
Total Revenue from Operations for the year (Total Sales)	12,00,000
Credit Revenue from Operations (Credit Sales) : 70% of Total Revenue from Operations	
Revenue from Operations Returns (Sales Returns) (out of Credit Revenue from Operations)	40,000
Opening Trade Receivables	73,250
Closing Trade Receivables	86,750

[Ans. Trade Receivables Turnover Ratio 10 Times; Average Collection Period 37 days.]

Q. 66. Calculate Trade Receivables Turnover Ratio and Average Collection Period from the following :—

	₹
Total Revenue from Operations for the year (Total Sales)	4,80,000
Cash Revenue from Operations (Cash Sales) : being 20% of Credit Revenue from Operations	
Opening Trade Receivables	60,000
Excess of Closing Trade Receivables over Opening Trade Receivables	30,000

[Ans. Trade Receivables Turnover Ratio 5.33 Times; Average Collection Period 68.48 days or 69 days.]

Working Notes :— (*i*) Credit Revenue from Operations = $\frac{100}{120}$ × ₹4,80,000.

(*ii*) Any fraction of a day would, in practice, mean next day.

Q. 67. Calculate Trade Receivables Turnover Ratio and Average Collection Period from the following figures :—

	₹
Total Revenue from Operations (Total Sales)	10,00,000
Cash Revenue from Operations (Cash Sales)	1,50,000
Revenue from Operations Return (Sales Returns)	10,000
Opening Debtors	50,000
Opening B/R	10,000
Closing Debtors	60,000
Closing B/R	20,000

[**Ans.** Trade Receivables Turnover Ratio 12 times; Average Collection Period 30.42 or 31 days.]

Q. 68. Calculate Debtors Turnover Ratio from the following information :

	₹
Credit Sales	22,00,000
Cash Received from Debtors	20,40,000
Discount Allowed	40,000
Sales Returns	60,000
Opening Debtors	4,70,000

[**Ans.** Closing Debtors ₹5,30,000; Debtors Turnover Ratio 4.28 times.]

Q. 69. From the following particulars determine the Opening Trade Receivables :

Credit Revenue from Operations (Credit Sales)	₹4,32,000
Trade Receivables turnover Ratio	12 Times
Closing Trade Receivables	₹40,000

[**Ans.** Opening Trade Receivables ₹32,000.]

Q. 70. Credit Revenue from Operations (Credit Sales) of *X* Ltd. during the year ended 31st March, 2020 were ₹5,64,000. If trade receivables turnover ratio is 6 times, calculate trade receivables in the beginning and at the end of the year. Trade Receivables at the end were ₹10,000 more than that at the beginning of the year.

[**Ans.** Opening Trade Receivables ₹89,000; Closing Trade Receivables ₹99,000.]

Q. 71. A Company made Credit Revenue from Operations (Credit Sales) of ₹8,76,000 during the year ended 31st March, 2020. If Trade Receivables Turnover Ratio is 18.25 times calculate :—

(I) Average Trade Receivables; and (II) Closing Trade Receivables, if closing Trade Receivables are three times in comparison to opening Trade Receivables.

[**Ans.** (I) Average Trade Receivables ₹48,000
(II) Closing Trade Receivables ₹72,000]

Q. 72. Calculate the amount of Opening Trade Receivables and Closing Trade Receivables from the following particulars :

Cost of Revenue from Operations	:	₹9,00,000
Gross Profit on Revenue from Operations	:	25%
Cash Revenue from Operations	:	20% of Credit Revenue from Operations
Trade Receivables Turnover Ratio	:	5 Times

Closing Trade Receivables were 3 times than that in the beginning.

[**Ans.** Opening Trade Receivables ₹1,00,000; Closing Trade Receivables ₹3,00,000.]

Q. 73. Calculate Closing Trade Receivables from the following information :

Cost of Revenue from Operations	:	₹16,00,000
Gross Profit on Cost	:	25%

Cash Revenue from Operations : 25% of Credit Revenue from Operations

Trade Receivables Turnover Ratio : 5 Times

Closing Trade Receivables were 1.5 times than that in the beginning.

[**Ans.** Closing Trade Receivables ₹3,84,000.]

Hint : Ratio between Opening and Closing Trade Receivables 2 : 3.

Q. 74. Following figures have been obtained from the books of Pawan Roadways Ltd :—

	2019 ₹	2020 ₹
Revenue from Operations (at Gross Profit of 25%)	36,00,000	60,00,000
Trade Receivables on 1st January	5,40,000	
Trade Receivables on 31st December	6,60,000	9,40,000
Inventory on 1st January	6,50,000	
Inventory on 31st December	7,00,000	10,00,000

Calculate the Trade Receivables Turnover Ratio. Also Calculate Inventory Turnover Ratio. Give necessary Comments.

[**Ans.** 2019 : Trade Receivables Turnover Ratio 6 times;

2020 : Trade Receivables Turnover Ratio 7.5 times;

Inventory Turnover Ratio in 2019 4 Times; in 2020 5.29 Times.]

Comments :— (1) In 2020, Trade Receivables Turnover Ratio has increased from 6 times to 7.5 times. It indicates that amount from trade receivables is being collected more quickly.

(2) In 2020, Inventory Turnover Ratio has also increased. It indicates that inventory is being rotated into Revenue from Operations more quickly. As such, the sales policy of the management is quite efficient.

Q. 75. Calculate Trade Payables Turnover Ratio and Average Payment Period from the following :

	₹
Total Purchases	24,00,000
Cash Purchases	6,40,000
Purchases Returns (out of credit purchases)	60,000
Opening Balance of Creditors	3,00,000
Opening Balance of Bills Payable	20,000
Closing Balance of Creditors	3,50,000
Closing Balance of Bills Payable	10,000

[**Ans.** Trade Payables turnover Ratio 5 times; Average Payment Period 73 days.]

Q. 76. Calculate Working Capital Turnover Ratio from the following information:

	₹
Current Assets	8,60,000
Current Liabilities	3,40,000

Cost of Revenue from Operations (Cost of Goods Sold)	20,00,000
Gross Profit	30% of Cost

[**Ans.** Working Capital Turnover Ratio : 5 times.]

Q. 77. Calculate Working Capital Turnover Ratio from the following information:

	₹
Inventory	3,10,000
Trade Receivables	1,30,000
Cash	20,000
Trade Payables	60,000
Cost of Revenue from Operations	30,40,000
G.P.	24% of Revenue from Operations

[**Ans.** Working Capital Turnover Ratio $= \frac{\text{Net Revenue from Operations}}{\text{Working Capital}} = 10$ Times.]

Q. 78. Determine the value of Current Liabilities of *Y* Ltd. from the following :

Cost of Revenue from Operations	₹ 6,00,000
Gross Profit	25% on Revenue from Operations
Current Assets	₹ 2,50,000
Working Capital Turnover Ratio	5 Times

[**Ans.** Current Liabilities ₹90,000]

Q. 79. Following information is given to you :

Trade Receivables on 1st April, 2014	₹6,80,000
Trade Receivables on 31st March, 2015	₹8,20,000
Trade Receivables Turnover Ratio	6 times
Credit Revenue from Operations	80% of Revenue from Operations
Working Capital Turnover Ratio	9 times
Current Ratio	2.25

Calculate :

(*i*) Revenue from Operations
(*ii*) Working Capital
(*iii*) Current Assets.

[**Ans.** (*i*) Revenue from Operations ₹56,25,000 (*ii*) Working Capital ₹6,25,000 (*iii*) Current Assets ₹11,25,000.]

Q. 80. Calculate Working Capital Turnover Ratio from the following :

	₹
Revenue from Operations	39,20,000
Non-Current Assets	21,00,000
Total Assets	36,00,000

Shareholder's Funds	18,00,000
Non-Current Liabilities	10,00,000

[Ans. 5.6 Times]

Q. 81. Calculate Working Capital Turnover Ratio from the following particulars :

	₹
Cost of Revenue from Operations	12,00,000
Gross Profit	20% of Revenue from Operations
Share Capital	5,00,000
General Reserve	1,50,000
Surplus *i.e.*, Balance in Statement of Profit & Loss	(20,000)
Long-term Borrowings	1,40,000
Long-term Provisions	50,000
Non-Current Assets	4,20,000

[Ans. Working Capital Turnover Ratio : 3.75 times.]

Q. 82. Following information is related to *X* Ltd. :—

	2019 ₹	*2020* ₹
Revenue from Operations	8,00,000	12,00,000
Gross Profit 25% on Revenue from Operations		

BALANCE SHEETS OF *X* LTD.

Particulars	*Note No.*	*31.3.2019*	*31.3.2020*
I. EQUITY AND LIABILITIES :		₹	₹
(1) Shareholder's Funds :			
(*a*) Share Capital		2,00,000	2,50,000
(*b*) Reserve and Surplus		1,65,000	1,72,000
(2) Non-Current Liabilities :			
Long-term Borrowings		60,000	40,000
(3) Current Liabilities :			
(*a*) Trade Payables		1,20,000	1,50,000
(*b*) Short-term Provision		20,000	10,000
TOTAL		5,65,000	6,22,000
II. ASSETS :			
(1) Non-Current Assets :			
Fixed Assets		2,85,000	3,50,000
(2) Current Assets :			
(*a*) Inventory		1,20,000	1,50,000
(*b*) Trade Receivables		80,000	75,000
(*c*) Cash and Bank Balance		75,000	45,000
(*d*) Other Current Assets (Prepaid Expenses)		5,000	2,000
TOTAL		5,65,000	6,22,000

Calculate the following ratios :

(*i*) Current Ratio; (*ii*) Quick Ratio; (*iii*) Inventory Turnover Ratio; (*iv*) Working Capital Turnover Ratio; and (*v*) Trade Receivables Turnover Ratio.

Ans.	*2019*	*2020*
(*i*) Current Ratio	1.96 : 1	1.69 : 1
(*ii*) Quick Ratio	1.11 : 1	.75 : 1
(*iii*) Inventory Turnover Ratio	5 Times	6.67 Times
(*iv*) Working Capital Turnover Ratio	5.71 Times	10.71 Times
(*v*) Trade Receivables Turnover Ratio	10 Times	15.48 Times

Profitability Ratios or Income Ratios :—

Q. 83 (A). Calculate Gross Profit Ratio from the following figures :—

Opening Inventory ₹40,000; Closing Inventory ₹60,000; Purchases ₹7,10,000; Return Outwards ₹10,000; Wages ₹80,000; Cash Revenue from Operations ₹3,45,000; Credit Revenue from Operations ₹6,30,000; Return Inward ₹25,000.

[**Ans.** G.P. Ratio 20%.]

Q. 83 (B). Calculate Gross Profit Ratio from the following figures :—

Cash Revenue from Operations ₹4,20,000; Credit Revenue from Operations ₹6,00,000; Revenue from Operations Returns (Sales Return) ₹20,000; Cost of Revenue from Operations ₹7,50,000.

[**Ans.** G.P. Ratio 25%.]

Q. 84. Calculate G.P. ratio from the following :—

	₹
Credit Revenue from Operations	2,40,000
Cash Revenue from Operations (being 20% of total Revenue from Operations)	
Purchases	2,20,000
Excess of opening inventory over closing inventory	14,000

[**Ans.** G.P. Ratio 22%.]

Q. 85. Calculate G.P. Ratio from the following :—

Credit Revenue from Operations were $\frac{1}{4}$th of Total Revenue from Operations. redit Revenue from Operations were ₹1,20,000. Credit Purchases were $\frac{1}{5}$th of Cash urchases. Credit Purchases were ₹40,000. Opening Inventory ₹70,000. It was 20,000 more than Closing Inventory; Carriage ₹15,000, Wages ₹45,000.

[**Ans.** G.P. Ratio 33.33%.]

Q. 86 (A). A company earns a gross profit of 25% on cost. Its credit Revenue from perations are twice its cash Revenue from Operations. If the credit Revenue from perations are ₹8,00,000, calculate the gross profit ratio of the company.

[**Ans.** G.P. Ratio 20%.]

Q. 86 (B). Gross Profit of a Company is 20% of Cost of Revenue from Operations. Its Cash Revenue from Operations are $\frac{1}{3}$rd of its Credit Revenue from Operations. Calculate the G.P. Ratio if the Cash Revenue from Operations are ₹3,00,000.

[**Ans.** G.P. Ratio 16.67%.]

Q. 87. Following information is available for the year ending 31st March, 2008, calculate gross profit ratio :

	₹
Cash Revenue from Operations	25,000
Credit Revenue from Operations	75,000
Purchases : Cash	15,000
Credit	60,000
Carriage Inwards	2,000
Salaries	25,000
Decrease in Inventory	10,000
Return Outwards	2,000
Wages	5,000

[**Ans.** G.P. Ratio 10%.]

Q. 88. Average Inventory ₹60,000; Inventory Turnover Ratio 5 Times; Revenue from Operations 40% above cost. Calculate Gross Profit Ratio.

[**Ans.** G.P. Ratio 28.57%]

Q. 89. Given the following information :

	₹
Revenue from Operations	3,40,000
Cost of Revenue from Operations	1,20,000
Selling Expenses	80,000
Administrative Expenses	40,000

Calculate Gross Profit Ratio and Operating Ratio.

[**Ans.** G.P. Ratio 64.71%; Operating Ratio 70.59%.]

Q. 90. Calculate operating ratio from the following :

	₹
Net Revenue from Operations	12,00,000
Credit Revenue from Operations	8,00,000
Gross Profit	3,00,000
Office Expenses	80,000
Selling Expenses	40,000
Loss by Fire	20,000

[**Ans.** Operating Ratio 85%.]

Hint : Net Revenue from Operations means Credit Revenue from Operations + Cash Revenue from Operations – Revenue from Operations Return.

Q. 91. Compute Operating Ratio from the following Statement of Profit and Loss of *X* Ltd. for the year ended 31st March, 2020 :

STATEMENT OF PROFIT AND LOSS
for the year ended 31st Marsh, 2020

Particulars	*Note No.*	₹
I. Revenue from Operations (Sales)		24,00,000
II. *Add* : Other Incomes		20,000
III. Total Revenue I + II		24,20,000
IV. *Less* : Expenses		
Cost of Materials Consumed		14,10,000
Change in Inventories of Finished Goods and Work in Progress		(30,000)
Employee Benefit Expenses		2,82,000
Finance Costs		20,000
Depreciation and Amortization Expenses		60,000
Other Expenses	1	1,20,000
Total Expenses		18,62,000
V. Profit before Tax (III – IV)		5,58,000

Notes to Accounts :

Particulars	₹
1. Other Expenses :	
Office Expenses	54,000
Loss by Fire	50,000
Donations	16,000
	1,20,000

[**Ans.** Operating Ratio 74%]

Q. 92. Calculate cost of Revenue from Operations from the following information

	₹
Operating Ratio	90%
Office Exp.	30,000
Selling Exp.	20,000
Revenue from Operations (Sales)	7,00,000
Revenue from Operations Return (Sales Returns)	40,000

[**Ans.** Cost of Revenue from Operations ₹5,44,000.]

Q. 93. Calculate (*i*) Operating Profit Ratio, and (*ii*) Net Profit Ratio from t following:—

	₹
Revenue from Operations	8,30,000

Return Inwards	30,000
Cost of Revenue from Operations	5,00,000
Office Expenses	40,000
Selling Expenses	18,000
Interest on Debentures	12,000
Loss by Accident	24,000
Interest received on Investments	10,000

[**Ans.** Operating Profit Ratio 30.25%. N.P. Ratio 27%.]

Q. 94. Calculate : (I) Gross Profit Ratio; (II) Operating Ratio; (III) Operating Profit Ratio; and (IV) Net Profit Ratio from the following :—

	₹
Revenue from Operations	2,00,000
Cost of Revenue from Operations	1,20,000
Administration Expenses	20,000
Selling Expenses	15,000
Loss by Fire	10,000
Income from Investments	5,000

[**Ans.** (I) G.P. Ratio 40%; (II) Operating Ratio 77.5%; (III) Operating Profit Ratio 22.5% and (IV) Net Profit Ratio 20%.]

Q. 95. Calculate (*i*) G.P. Ratio, (*ii*) Operating Ratio, (*iii*) Operating Profit Ratio, (*iv*) Inventory Turnover Ratio, and (*v*) Working Capital Turnover Ratio from the following figures :

	₹
Purchases	18,30,000
Direct Expenses	4,10,000
Opening Inventory	3,60,000
Closing Inventory	4,40,000
Operating Expenses	5% of Sales
Revenue from Operations	30,00,000
Current Assets (including inventory)	7,00,000
Current Liabilities	2,00,000

[**Ans.** (*i*) 28% (*ii*) 77% (*iii*) 23% (*iv*) 5.4 times (*v*) 6 times.]

Q. 96. Gross Profit ratio of a Company was 25%. Its cash Revenue from Operations were ₹5,00,000 and its credit Revenue from Operations were 90% of the total Revenue from Operations. If the indirect expenses of the company were ₹1,50,000, calculate its net profit ratio.

[**Ans.** Net Profit Ratio 22%.]

Q. 97. Calculate Net Profit Ratio from the following information :

Revenue from Operations ₹25,00,000; Operating Ratio 90%; Loss on Sale of Fixed Assets ₹25,000; Interest on Long term Borrowings ₹30,000; Income from Investments ₹40,000.

[**Ans.** Net Profit Ratio : 9.4%.]

Q. 98. Calculate the earning per share and price earning ratio from the following data :

	₹
Equity Share Capital (₹10 per share)	2,00,000
10% Preference Share Capital (₹100 each)	1,50,000
Net Profit after deduction of tax	95,000
Market Price of Equity Share	64

[**Ans.** Earning Per Share ₹4; Price Earning Ratio 16 times.]

Q. 99. *X* Ltd. submits following informations :

	₹
8% Preference Share Capital	5,00,000
Equity Share Capital (2,50,000 shares of ₹10 each)	25,00,000
Profit before tax	14,00,000
Tax rate	40%
Market Price of Equity Share	40

Compute (*i*) Earning Per Share (*ii*) Price Earning Ratio.

[**Ans.** (*i*) ₹3.20 per share (*ii*) 12.5 times]

Q. 100. Following is the Balance Sheet of Ganesh Ltd. as at 31st March, 2018 :

Particulars	*Note No.*	₹
I. EQUITY AND LIABILITIES :		
Shareholder's Funds :		
(*a*) Share Capital		30,00,000
(*b*) Reserve & Surplus	1	23,00,000
Non-Current Liabilities :		
Long-term Borrowings	2	22,00,000
Current Liabilities :		
Trade Payables		4,00,000
TOTAL		79,00,000
II. ASSETS :		
Non-Current Assets :		
Fixed Assets		55,00,000
Current Assets :		
(*a*) Inventory		12,00,000
(*b*) Trade Receivables		9,00,000
(*c*) Cash & Bank Balance		3,00,000
TOTAL		79,00,000

Notes : (1) Reserve & Surplus :

Reserve	13,00,000
Profit for the year	10,00,000
	23,00,000

(2) Long-term Borrowings :

8% Loans	10,00,000
10% Debentures	12,00,000
	22,00,000

Calculate 'Return on Capital Employed'.

[**Ans.** Return on Capital Employed 16%.]

Q. 101. Calculate Return on Capital Employed from the following :

	₹
Share Capital	7,20,000
Reserves & Surplus	6,50,000
Current Liabilities	7,50,000
Non Current Assets	15,00,000
Inventory	5,00,000
Trade Receivables	6,00,000
Cash & Bank Balance	1,00,000
10% Long term Borrowings	5,00,000
Long term Provisions	80,000

Net Profit before Tax ₹2,50,000

[**Ans.** 15.38%]

Q. 102. Net Profit after Interest but before Tax ₹65,000; Shareholder's Funds ₹3,00,000; 15% Long-Term Debt ₹1,00,000. Calculate Return on Investment.

[**Ans.** 20%.]

Note : It is assumed that Shareholder's Funds include current year's profits.

Q. 103. Net Profit after Interest and Tax of *M* Ltd. was ₹1,00,000. Its Current Assets were ₹4,00,000 and Current Liabilities were ₹2,00,000. Tax rate was 50%. Its Total Assets were ₹10,00,000 and 10% Long term debt was ₹4,00,000.

Calculate Return on Investment. *(C.B.S.E. 2019 Comptt.)*

[**Ans.** Return on Investment 30%.]

Hints (*i*) Capital Employed = Total Assets – Current Liabilities.

(*ii*) Current Assets will be ignored.

Q. 104. Calculate 'Return on Capital Employed' from the following details :—

Gross Profit ₹2,70,000; Administration Expenses ₹60,000; Selling Expenses ₹30,000; 12% Long-Term Debts ₹2,00,000; Tax Rate 40%; Non Current Assets ₹6,00,000; Current Assets ₹2,00,000; and Current Liabilities ₹50,000.

[**Ans.** R.O.I. 24%.]

Q. 105. Calculate Return on Investment from the following :—

	₹
Non Current Assets	2,00,000
Current Assets	1,50,000
Current Liabilities	50,000
Opening Inventory	40,000
Closing Inventory	60,000
Purchases	6,00,000

Carriage Inwards	15,000
Revenue from Operations	7,00,000
Office Expenses	30,000
Interest on Debentures	12,000
Tax	7,000

[**Ans.** R.O.I. 25%.]

Hint :— Profit before Interest and Tax = ₹75,000.

Q. 106. Calculate Return on Investment from the following details :—

	₹
Equity Share Capital	5,00,000
12% Preference Share Capital	1,00,000
Reserves	1,44,000
15% Loans	2,40,000
10% Debentures	1,20,000
Current Liabilities	75,000
Net Profit (after Interest and Income Tax)	96,000
Rate of Income Tax	50%

[**Ans.** R.O.I. 20%.]

Q. 107. A Company has a loan of ₹30,00,000 as part of its capital employed. Interest payable on the loan is 12% and the R.O.I. of the company is 25%. The rate of income tax is 40%. What is the gain to shareholders due to the loan raised by the company?

[**Ans.** Net gain to shareholders ₹2,34,000.]

Q. 108. On the basis of the following information calculate (*i*) Liquid Ratio, (*ii*) Gross Profit Ratio and (*iii*) Operating Ratio :

	₹
Net Working Capital	17,600
Current Assets	39,600
Inventories	23,100
Revenue from Operations	1,50,000
Cost of Revenue from Operations	1,02,000
Operating Expenses	18,000

[**Ans.** (*i*) Liquid Ratio .75, (*ii*) Gross Profit Ratio 32%, (*iii*) Operating Ratio 80%.]

Q. 109. Calculate any three of the following ratios with the help of the following information :

(*i*) Operating Ratio, (*ii*) Current Ratio, (*iii*) Gross Profit Ratio, (*iv*) Inventory Turnover Ratio; and (*v*) Debt Equity Ratio.

Information : Equity Share Capital ₹5,00,000; 12% Debentures ₹6,00,000; 9% Preference Share Capital ₹3,00,000; Reserve & Surplus ₹1,00,000; Revenue from Operations ₹10,00,000; Opening Inventory ₹80,000; Purchases ₹6,00,000; Wages

₹1,00,000; Closing Inventory ₹1,00,000; Selling and distribution expenses ₹ 20,000; Other current assets ₹5,00,000 and Current liabilities ₹3,00,000.

[**Ans.** (*i*) 70%; (*ii*) 2 : 1; (*iii*) 32%; (*iv*) 7.56 times; (*v*) .67 : 1.]

Hint : Reserve and Surplus includes current year's Net Profit also.

Q. 110. From the following information, calculate the following ratios :—

(*i*) Debt-Equity Ratio;
(*ii*) Proprietary Ratio;
(*iii*) Working Capital Turnover Ratio;
(*iv*) Interest Coverage Ratio;

Information :—

	₹
Equity Share Capital	1,20,000
10% Preference Share Capital	40,000
General Reserve	1,60,000
Loan @ 15% interest	2,00,000
Revenue from Operations for the year	5,60,000
Tax paid during the year	40,000
Profit for the current year after interest and tax	80,000
Fixed Assets	5,20,000
Current Assets	1,05,000
Current Liabilities	25,000

[**Ans.** (*i*) .5 : 1; (*iii*) 7 Times; (*iv*) 5 Times; (*v*) 20% and (*vi*) 21.11%]

Hints :— (*i*) Debt Equity Ratio $= \frac{\text{Long term Debts}}{\text{Shareholder's Funds}}$

(*ii*) Shareholder's Funds = Equity Share Capital + Pref. Share Capital + General Reserve + Current Year's Profit = ₹4,00,000.

ADDITIONAL QUESTIONS
(For Practice)

Liquidity Ratios :—

Q. 111. Current Liabilities of a Company were ₹80,000 and its Current Ratio was 2.5 : 1. After this, it purchased goods for ₹40,000 on credit. Calculate the revised Current Ratio.

[**Ans.** 2 : 1.]

Q. 112. Current Assets of a Company are ₹3,06,000 and its Current ratio is 1.8. Afterwards, it issued new equity shares of ₹1,00,000. Calculate the revised current ratio.

[**Ans.** 2.388.]

Q. 113. The Current Ratio of a Company is 0.8 : 1. State giving reasons which of the following transactions would (*i*) Improve; (*ii*) Reduce; (*iii*) Not change; the Current Ratio :

(*a*) Payment of Trade Payables.
(*b*) Purchase of goods on Credit.
(*c*) Sale of furniture costing ₹10,000 at a loss of ₹2,000.
(*d*) Sale of goods costing ₹15,000 at a profit of ₹1,000.
(*e*) Payment of dividend payable.

[**Ans.** (*a*) Reduce; (*b*) Improve; (*c*) Improve; (*d*) Improve; (*e*) Reduce.]

Q. 114. The Quick Ratio of a Company is 1.5 : 1. State giving reasons which of the following transactions would (*i*) Improve; (*ii*) Reduce; (*iii*) Not change; the Quick Ratio :

(*a*) Payment of Trade Payables.
(*b*) Purchase of goods for Cash.
(*c*) Purchase of goods on Credit.
(*d*) Sale of goods Costing ₹50,000 for ₹50,000.
(*e*) Sale of goods Costing ₹50,000 for ₹45,000.
(*f*) Cash received from Trade Receivables.

[**Ans.** (*a*) Improve; (*b*) Reduce; (*c*) Reduce; (*d*) Improve; (*e*) Improve; (*f*) Not change.]

Q. 115. Current Assets ₹5,00,000; Working Capital ₹3,00,000. Calculate Current Ratio.

[**Ans.** 2.5 : 1.]

Hint :— Current Assets – Working Capital = Current Liabilities.

Q. 116. Current Liabilities ₹20,000; Working Capital ₹80,000. Calculate Current Ratio.

[**Ans.** 5 : 1.]

Q. 117. Current Ratio 3 : 1; Current Assets ₹60,000. Calculate Current Liabilities.

[**Ans.** ₹20,000.]

Q. 118. Current Ratio 4.2 : 1; Current Liabilities ₹2,00,000. Calculate Current Assets.

[**Ans.** ₹8,40,000.]

Q. 119. Quick Ratio 2 : 1; Current Liabilities ₹2,00,000; Inventory ₹1,60,000. Calculate Current Ratio.

[**Ans.** 2.8 : 1.]

Q. 120. Quick Ratio 1.6 : 1; Liquid Assets ₹4,80,000; Inventory ₹1,50,000. Calculate Current Ratio.

[**Ans.** 2.1 : 1.]

Q. 121. Quick Ratio 3; Current Assets ₹2,50,000; Inventory ₹40,000. Calculate Current Liabilities.

[**Ans.** ₹70,000.]

Q. 122. Quick Ratio 2.2; Current Liabilities ₹40,000; Inventory ₹32,000. Calculate Current Assets.

[**Ans.** ₹1,20,000.]

Q. 123. Current Assets ₹1,00,000; Inventory ₹55,000; Working Capital ₹70,000. Calculate Quick Ratio.

[**Ans.** 1.5 : 1.]

Q. 124. Current Liabilities ₹80,000; Working Capital ₹1,70,000; Inventory ₹85,000; Prepaid Expenses ₹5,000. Calculate Quick Ratio.

[**Ans.** 2 : 1.]

Q. 125. Current Ratio 3 : 1; Working Capital ₹4,00,000; Inventory ₹2,50,000. Calculate Current Assets, Current Liabilities, Quick Ratio.

[**Ans.** Current Assets ₹6,00,000; Current Liabilities ₹2,00,000; Quick Ratio 1.75 : 1.]

Q. 126. Current Ratio 3 : 1; Acid Test Ratio 0.9 : 1; Current Liabilities ₹1,20,000. Calculate Current Assets; Liquid Assets and Inventory.

[**Ans.** Current Assets ₹3,60,000; Liquid Assets ₹1,08,000 and Inventory ₹2,52,000.]

Q. 127. Current Ratio 2.5 : 1; Quick Ratio 1 : 1; Current Assets ₹5,00,000. Calculate Current Liabilities; Liquid Assets and Inventory.

[**Ans.** Current Liabilities ₹2,00,000; Liquid Assets ₹2,00,000 and Inventory ₹3,00,000.]

Q. 128. Current Ratio 3 : 1; Quick Ratio 1.2 : 1; Working Capital ₹1,50,000. Calculate Current Assets, Current Liabilities and Inventory.

[**Ans.** Current Assets ₹2,25,000; Current Liabilities ₹75,000 and Inventory ₹1,35,000.]

Q. 129. Calculate Liquid Ratio from the following (upto two decimal places) :

Current Assets	₹1,26,000
Inventories	₹2,000
Current Ratio	3 : 2

(ISC 2016)

[**Ans.** 1.48 : 1.]

Q. 130. The ratio of Current Assets (₹9,00,000) to Current Liabilities is 1.5 : 1. The accountant of this firm is interested in maintaining a Current Ratio of 2 : 1 by paying some part of Current Liabilities. You are required to suggest him the amount of Current Liabilities which must be paid for this purpose.

[**Ans.** ₹3,00,000.]

Solvency Ratios :—

Q. 131. Calculate Current Ratio, Quick Ratio, Debt-Equity Ratio and the Proprietary Ratio from the figures given below :—

	₹
Inventory	30,000
Prepaid Expenses	2,000
Liquid Assets	50,000

Current Liabilities	40,000
12% Debentures	30,000
Accumulated Profits	10,000
Equity Share Capital	1,00,000
Long term investments	15,000
Fixed Assets	83,000

[**Ans.** (*i*) Current Ratio 2.05 : 1; (*ii*) Quick ratio 1.25 : 1; (*iii*) Debt-Equity Ratio .27 : 1; (*iv*) Proprietary Ratio i.e. $\frac{\text{Shareholder's Funds}}{\text{Total Assets}} = 61.11\%$.]

Q. 132. From the following details, calculate Inventory Turnover Ratio :

Annual Revenue from Operations		₹2,00,000
Gross Profit Rate		25% on revenue from operations
Inventory :	Opening	₹ 38,500
	Closing	₹ 41,500

[**Ans.** Inventory Turnover Ratio 3.75 Times.]

Hint :— Gross Profit = ₹2,00,000 × $\frac{25}{100}$

Q. 133. From the following details, calculate Inventory Turnover Ratio :—

Annual Revenue from Operations		₹2,00,000
Gross Profit Rate		25% on Cost
Inventory :	Opening	₹ 38,500
	Closing	₹ 41,500

[**Ans.** Inventory Turnover Ratio 4 Times.]

Hint :— Gross Profit = ₹2,00,000 × $\frac{25}{125}$.

Q. 134. Opening Inventory ₹40,000; Closing Inventory ₹50,000; Revenue from Operations ₹8,00,000; Gross Profit Ratio 20%. Calculate Inventory Turnover Ratio. *(I.S.C. 2013)*

[**Ans.** 14.22 Times.]

Q. 135. Opening Inventory ₹29,000; Purchases ₹2,42,000; Revenue from Operations ₹3,20,000; Gross Profit Ratio is 25% on revenue from operations. Calculate Inventory Turnover ratio.

[**Ans.** Cost of Revenue from Operations ₹2,40,000; Inventory Turnover Ratio 8 Times.]

Iint :— Calculation of Closing Inventory :

Cost of Revenue from Operations = Opening Inventory + Purchases – Closing Inventory
Ience, Closing Inventory = Opening Inventory + Purchases – Cost of Revenue from Operations
= 29,000 + 2,42,000 – 2,40,000
= ₹31,000

Q. 136. Closing Inventory ₹22,000; Purchases ₹1,48,000; Purchase Return ₹8,000; Carriage ₹4,000; Revenue from Operations (Sales) ₹1,90,000; Revenue from Operations Return (Sales Returns) ₹10,000; Gross Profit 20% on Cost. Calculate Inventory Turnover Ratio.

[**Ans.** Cost of Revenue from Operations ₹1,50,000; Inventory Turnover Ratio 6 Times.]

Hint :— Calculation of Opening Inventory :

Cost of Revenue from Operations = Opening Inventory + Purchases + Carriage – Closing Inventory

Hence, Opening Inventory = Cost of Revenue from Operations – Purchases – Carriage + Closing Inventory
= 1,50,000 – 1,40,000 – 4,000 + 22,000
= ₹28,000

Q. 137. Find out the value of opening inventory from the following particulars :—

Total Revenue from Operations	₹2,00,000
Inventory Turnover Ratio	5 Times
Gross Profit	25% on Revenue from Operations

You are informed that closing inventory is ₹8,000 more than the opening inventory.

[**Ans.** Value of opening inventory ₹26,000.]

Q. 138. ₹6,30,000 is the cost of Revenue from Operations of a firm for the year 2020. If inventory turnover ratio is 7 times, calculate inventory at the end of the year. Inventory at the end is twice than that in the beginning.

[**Ans.** Inventory at the end ₹1,20,000.]

Hint : Average inventory is worked out at ₹90,000. Therefore, the total of opening inventory and closing inventory = 90,000 × 2 = 1,80,000. If this figure is divided in the ratio of 1 : 2, the opening inventory will be ₹60,000 and closing inventory ₹1,20,000.

Q. 139. Following figures have been extracted from Shivalika Mills Ltd. :—

Inventory in the beginning of the year	₹ 60,0
Inventory at the end of the year	₹1,00,000
Inventory turnover ratio	8 times
Revenue from Operations	25% above cost

Compute the amount of gross profit and Revenue from Operations.

[**Ans.** G.P. ₹1,60,000; Revenue from Operations ₹8,00,000.]

Q. 140. Calculate current assets of a company from the following information :

(*i*) Inventory turnover 4 times.
(*ii*) Inventory in the end is ₹20,000 more than inventory in the beginning.
(*iii*) Revenue from Operations ₹3,00,000.
(*iv*) Gross profit ratio 20%.
(*v*) Current liabilities ₹40,000
(*vi*) Quick ratio 0.75.

[**Ans.** Current Assets ₹1,00,000.]

Hint :— Closing Inventory ₹70,000.

Q. 141. Following are the details available :—

	₹
Current Assets	1,00,000
Current Liabilities	70,000
Total Revenue from Operations (Total Sales)	2,00,000
Cost of Revenue from Operations (Cost of Goods Sold)	1,50,000
Operating Expenses	20,000
Inventory turnover	5 times

If the closing inventory is more by ₹4,000 than opening inventory, determine the following :—

(*i*) Opening Inventory,
(*ii*) Liquid Ratio.

[**Ans.** (*i*) Opening Inventory ₹28,000; (*ii*) Liquidity Ratio .97 : 1.]

Q. 142. From the following information, calculate trade receivables turnover ratio and average collection period :—

	₹
Credit Revenue from Operations (Credit Sales)	14,80,000
Revenue from Operations Returns (Sales Returns)	20,000
Debtors	2,50,000
Bills Receivable	42,000
Provision for Doubtful Debts	1,500

[**Ans.** Trade Receivables turnover Ratio 5 times; Average Collection Period 73 days.]

Hint : Provision for Doubtful Debts is not deducted from Trade Receivables for the alculation of this ratio.

Q. 143. Closing Trade Receivables ₹4,00,000; Cash Revenue from Operations being 25% of Credit Revenue from Operations. Excess of Closing Trade Receivables over Opening Trade Receivables ₹2,00,000. Total Revenue from Operations ₹15,00,000. Calculate Trade Receivables Turnover Ratio.

[**Ans.** 4 Times.]

Q. 144. Opening Trade Receivables ₹3,60,000; Cash Revenue from Operations being 20% of Credit Revenue from Operations. Excess of Closing Trade Receivables over Opening Trade Receivables ₹60,000. Cost of Revenue from Operations ₹18,00,000; Gross Profit ₹5,40,000. Calculate Trade Receivables Turnover Ratio.

[**Ans.** 5 Times.]

Q. 145. Opening Trade Receivables ₹10,000; Total Revenue from Operations Total Sales) ₹4,00,000; Cash Revenue from Operations being $\frac{2}{5}$th of Total Revenue rom Operations; Revenue from Operations Return (Sales Returns) ₹60,000 ($\frac{1}{3}$rd out of Cash Revenue from Operations); Closing Trade Receivables were four times than hat in the beginning. Calculate Trade Receivables Turnover Ratio and Average Collection Period.

[**Ans.** Trade Receivables Turnover Ratio 8 Times; Average Collection Period 46 days.]

Q. 146. Calculate amount of Opening Trade Receivables and Closing Trade Receivables from the following figures :

Trade Receivable Turnover ratio	5 Times
Cost of Revenue from Operations	₹8,00,000
Gross Profit Ratio	20%

Closing Trade Receivables were ₹40,000 more than in the beginning.
Cash sales being 1/4 times of Credit Sales. *(C.B.S.E. Sample Paper, 2019)*

[**Ans.** Opening Trade Receivables ₹1,40,000; Closing Trade Receivables ₹1,80,000.]

Q. 147. Calculate the amount of Opening Trade Receivables and Closing Trade Receivables from the following :—

Trade Receivables Turnover Ratio	10 times
Cost of Revenue from Operations	₹7,00,000
G.P. Ratio	30% of Revenue from Operations

You are informed that Closing Trade Receivables were three times than that in the beginning. Cash Revenue from Operations being 25% of Credit Revenue from Operations.

[**Ans.** Opening Trade Receivables ₹40,000; Closing Trade Receivables ₹1,20,000.]

Working Notes :

(*i*) Total Revenue from Operations $= 7{,}00{,}000 \times \frac{100}{70} =$ ₹10,00,000

(*ii*) Credit Revenue from Operations $= 10{,}00{,}000 \times \frac{100}{125} =$ ₹8,00,000

(*iii*) Average Trade Receivables $= \frac{8{,}00{,}000}{10} =$ ₹80,000

(*iv*) Total of Opening Trade Receivables and Closing Trade Receivables
$=$ ₹$80{,}000 \times 2 =$ ₹1,60,000

(*v*) If this figure of ₹1,60,000 is divided in the ratio of 1 : 3, the amount of opening Trade Receivables and Closing Trade Receivables will be found out.

Q. 148. From the following particulars determine the Closing Trade Receivables :

	₹
Total Revenue from Operations	24,00,000
Cash Revenue from Operations	4,60,000
Sales Returns (out of credit Revenue from Operations)	20,000
Trade Receivables Turnover Ratio	6 Times
Opening Debtors	2,50,000
Opening B/R	14,000
Closing B/R	12,000

[**Ans.** Closing Debtors ₹3,64,000.]

Hint :— Average Debtors and B/R ₹3,20,000.

Profitability Ratios or Income Ratios :—

Q. 149. Calculate G.P. Ratio from the following :—

	₹
Credit Revenue from Operations	6,00,000
Cash Revenue from Operations (Being 25% of Total Revenue from Operations)	
Purchases	6,90,000
Excess of Closing Inventory over Opening Inventory	50,000

[Ans. G.P. Ratio 20%.]

Q. 150. Calculate Gross Profit Ratio from the following data :—

	₹
Credit Revenue from Operations	2,00,000
Cash Revenue from Operations (being $33\frac{1}{3}\%$ of Total Revenue from Operations)	
Purchases	2,25,000
Carriage Inwards	25,000
Excess of Closing Inventory over Opening Inventory	10,000

[Ans. G.P. Ratio 20%.]

Hint :— Total Revenue from Operations $= \frac{100}{66\frac{2}{3}} \times 2,00,000$

$= 100 \times \frac{3}{200} \times 2,00,000 = 3,00,000.$

Q. 151. Calculate G.P. Ratio from the following :—

Cash Revenue from Operations are $\frac{1}{3}$rd of total Revenue from Operations. Cash revenue from Operations were ₹6,00,000; Credit Purchases are 25% of total purchases. Credit Purchases were ₹3,00,000. Opening Inventory ₹1,00,000; Closing Inventory was ₹50,000 more than Opening Inventory. Carriage ₹15,000. Wages ₹35,000.

[Ans. G.P. Ratio 33.33%.]

Q. 152. From the following informations calculate :

(*a*) Current Ratio,
(*b*) Quick Ratio,
(*c*) Operating Ratio, and
(*d*) Gross Profit Ratio

	₹		₹
Current Assets	70,000	Operating Expenses	40,000
Current Liabilities	35,000	Revenue from Operations	1,20,000
Inventory	30,000	Cost of Revenue from Operations	60,000

[Ans. (*a*) 2 : 1; (*b*) 1.14 : 1; (*c*) 83.33%; (*d*) 50%.]

Q. 153. Calculate Gross Profit Ratio from the following information :

Particulars	₹
Opening Inventory	80,000

Closing Inventory	1,00,000
Revenue from Operations	9,00,000
Inventory Turnover Ratio	8 Times

[**Ans.** G.P. Ratio 20%] *(I.S.C. 2019)*

Q. 154. A trader carries an average inventory of ₹40,000. His inventory turnover Ratio is 8 times. If he sells goods at a profit of 20% on Revenue from Operations, find out his profit.

[**Ans.** Gross Profit ₹80,000.]

Hint :— Cost of Revenue from Operations ₹3,20,000.

Q. 155. From the following data, calculate :—

(*i*) Gross Profit Ratio; (*ii*) Operating Ratio; (*iii*) Net Profit Ratio; (*iv*) Inventory turnover Ratio; and (*v*) Current Ratio.

	₹		₹
Revenue from Operations	25,20,000	Fixed Assets	14,40,000
Cost of Revenue from Operations	19,20,000	Net worth	15,00,000
Operating Expenses	2,40,000	Debt (Long-Term)	9,00,000
Average Inventory	8,00,000	Current Liabilities	6,00,000

[**Ans.** (*i*) G.P. Ratio 23.81%; (*ii*) Operating Ratio 85.71%; (*iii*) N.P. Ratio 14.29%; (*iv*) Inventory Turnover Ratio 2.4 times; and (*v*) Current Ratio 2.6 : 1.]

Hint : Current Assets = Net Worth + Long Term Debts + Current Liabilities – Fixed Assets.

Q. 156. From the following data, calculate :—

(*i*) Gross Profit Ratio,
(*ii*) Net Profit Ratio
(*iii*) Working Capital Turnover Ratio,
(*iv*) Debt-Equity Ratio,
(*v*) Proprietary Ratio.

	₹
Revenue from Operations	30,00,000
Cost of Revenue from Operations	20,00,000
Net Profit	3,00,000
Fixed Assets	6,50,000
Current Assets	6,00,000
Current Liabilities	2,00,000
Paid-up Share Capital	5,00,000
Debentures	2,50,000

[**Ans.** G.P. Ratio $33\frac{1}{3}$ % ; N.P. Ratio 10%; Working Capital Turnover Ratio 7.5 Times; Debt-Equity Ratio .31 : 1; Proprietary Ratio *i.e* $\frac{\text{Shareholder's Funds}}{\text{Total Assets}}$ = 64%.]

Q. 157. The following information is given about a company :—

	₹
Revenue from Operations	1,50,000
Gross Profit	30,000
Operating Exp.	7,500
Opening Inventory	29,000
Closing Inventory	31,000
Trade Receivables	16,000
Net Fixed Assets	1,10,000

From the above information, calculate the following ratios :—

(*i*) Gross Profit Ratio.
(*ii*) Operating Ratio.
(*iii*) Inventory Turnover Ratio.
(*iv*) Trade Receivables Turnover Ratio.

[**Ans.** (*i*) 20%; (*ii*) 85%; (*iii*) 4 times; (*iv*) 9.375 times.]

Q. 158. With the help of the given information, calculate any three of the following ratios : (*i*) Operating ratio, (*ii*) Quick ratio, (*iii*) Working capital turnover ratio, and (*iv*) Debt equity ratio.

Information : Equity Share Capital ₹50,000; 12% Preference Share Capital ₹40,000; 12% Debentures ₹30,000; Reserve and Surplus ₹40,000; Sales ₹3,00,000; Opening Inventory ₹20,000; Purchases ₹1,40,000; Wages ₹30,000; Closing Inventory ₹40,000; Selling and distribution expenses ₹18,000; Trade Receivables ₹75,000; Cash & Bank Balance ₹25,000 and Current Liabilities ₹60,000.

[**Ans.** (*i*) 56%; (*ii*) 1.67 : 1; (*iii*) 3.75 Times; (*iv*) .23 : 1]

Hints : (1) Working Capital = Closing Inventory + Trade Receivables + Cash & Bank Balance – Current liabilities.
(2) Reserve and Surplus includes Current year's net profit also.

Q. 159. From the following information :

	₹
Opening inventory	5,00,000
Fixed Assets	5,25,000
Cost of Revenue from Operations	18,00,000
Revenue from Operations	30,00,000
Operating expenses	4,80,000
Interest Charges	1,80,000
Current liabilities	6,00,000
Current Assets	9,75,000
Closing inventory	7,00,000

Calculate any three of the following :

(*i*) Operating ratio
(*ii*) Inventory turnover ratio

(*iii*) Net Profit Ratio, and
(*iv*) Liquid Ratio.

[**Ans.** Operating Ratio 76%; Inventory Turnover Ratio 3 Times; Net Profit Ratio 18%; and Liquid Ratio .46 : 1]

Hint : Capital Employed = Fixed Assets + Current Assets – Current Liabilities.

Q. 160. On the basis of information given below, calculate any two of the following ratios :

(*i*) Gross Profit Ratio;
(*ii*) Debt-Equity Ratio, and
(*iii*) Working Capital Turnover Ratio.

Information :

	₹		₹
Revenue from Operations	3,75,000	Current Assets	4,25,000
Cost of Revenue from Operations	2,50,000	Equity Share Capital	1,90,000
Current Liabilities	1,20,000	Debentures	75,000
Loan	60,000		

[**Ans.** Gross Profit Ratio $33\frac{1}{3}$%; Debt-Equity Ratio 0.71 : 1; Working Capital Turnover Ratio 1.23 times.]

Q. 161. On the basis of the following information, calculate the following ratios :

(*a*) Operating Ratio
(*b*) Liquid Ratio
(*c*) Proprietary Ratio

Information :

Cash Revenue from Operations ₹4,00,000; Credit Revenue from Operations ₹2,75,000; Revenue from Operations Returns (Sales Returns) ₹27,000; Cost of Revenue from Operations ₹3,90,000; Selling and Distribution Expenses ₹7,000; Administration Expenses ₹3,000; Current Liabilities ₹1,95,000; Current Assets ₹3,94,000; Closing Inventory ₹23,000; Equity Share Capital ₹4,37,000; 6% Preference Share Capital ₹1,74,000; Fixed Assets ₹4,30,000.

[**Ans.** (*a*) 61.73%; (*b*) 1.9 : 1; (*c*) 74.15%.]

Q. 162. The current ratio of a company is 2 : 1. State which of the following would improve, reduce or not change the ratio :

(*i*) Repayment of a current liability.
(*ii*) Purchasing goods on credit.
(*iii*) Sale of motor vehicle at a profit of 10%.
(*iv*) Sale of goods at a profit of 10%.
(*v*) Payment of dividend payable.
(*vi*) Repayment of Long term Borrowings

[**Ans.** (*i*) Improve; (*ii*) Reduce; (*iii*) Improve; (*iv*) Improve; (*v*) Improve and (*vi*) Reduce.]

Q. 163. From the following information calculate the following ratios :

(*i*) Current Ratio
(*ii*) Debt Equity Ratio
(*iii*) Operating Ratio

Revenue from Operations ₹1,00,000; Cost of Revenue from Operations was 80% of Revenue from Operations; Equity Share Capital ₹7,00,000; Reserve and Surplus ₹3,00,000; Operating Expenses ₹10,000; Quick Assets ₹6,00,000; 9% Debentures ₹5,00,000; Closing Inventory ₹50,000; Prepaid Expenses ₹10,000 and Current Liabilities ₹4,00,000.

[**Ans.** Current Ratio 1.65 : 1; Debt Equity Ratio 0.5 : 1; Operating Ratio 90%.]

Hint : Reserve and Surplus includes Current Year's Net Profit also.

Q. 164. From the following information, calculate the following ratios:

(*i*) Operating Ratio
(*ii*) Inventory Turnover Ratio
(*iii*) Proprietary Ratio

Information :

Cash Revenue from Operations : ₹10,00,000
Credit Revenue from Operations : 120% of Cash Revenue from Operations
Operating Expenses : 10% of Total Revenue from Operations
Rate of Gross Profit : 40%
Opening Inventory : ₹1,50,000
Closing Inventory : ₹20,000 *more* than Opening Inventory
Current Assets : ₹3,00,000
Current Liabilities : ₹2,00,000
Share Capital : ₹6,00,000
Fixed Assets : ₹5,00,000

[**Ans.** (*i*) 70%; (*ii*) 8.25 times; (*iii*) 75%.]

Q. 165. From the following information, calculate the following ratios:

(*i*) Liquid Ratio
(*ii*) Gross Profit Ratio
(*iii*) Debt-Equity Ratio

Information :

Revenue from Operations : ₹4,00,000
Opening Inventory : ₹10,000
Closing Inventory : ₹3,000 *less* than Opening Inventory
Net Purchases : 80% of Revenue from Operations
Direct Expenses : ₹20,000
Current Assets : ₹1,00,000
Prepaid Expenses : ₹3,000
Current Liabilities : ₹60,000
9% Debentures : ₹4,00,000
Long term loan from Bank : ₹1,50,000

Equity Share Capital	: ₹8,00,000
8% Preference Share Capital	: ₹3,00,000

[**Ans.** (*i*) Liquid Ratio 1.5 : 1; (*ii*) Gross Profit Ratio 14.25%; (*iii*) Debt Equity Ratio .5 : 1.]

Hint : Liquid Assets = Current Assets – Closing Inventory – Prepaid Exp.
= 1,00,000 – 7,000 – 3,000 = ₹90,000

Q. 166. From the following information, calculate the following ratios:

(*i*) Liquid Ratio;
(*ii*) Inventory Turnover Ratio; and
(*iii*) Return on Investment.

	₹
Inventory in the beginning	50,000
Inventory at the end	60,000
Revenue from Operations	4,00,000
Gross Profit	1,94,000
Cash and Cash Equivalents	40,000
Trade Receivables	1,00,000
Trade Payables	1,90,000
Other Current Liabilities	70,000
Share Capital	2,00,000
Reserves and Surplus (Balance in the Statement of Profit & Loss)	1,40,000

(N.C.E.R.T.)

[**Ans.** (*i*) Liquid Ratio 0.54 : 1; (*ii*) Inventory Turnover Ratio 3.75 times; (*iii*) Return on Investment 41.18%.]

Q. 167. From the given information, calculate the following ratios :—

(*i*) Debt-Equity Ratio;
(*ii*) Debt to Total Assets Ratio
(*iii*) Operating Ratio
(*iv*) Trade Receivables Turnover Ratio
(*v*) Trade Payables Turnover Ratio

	₹
Shareholders' Funds	50,000
10% Debentures	25,000
Total Assets	1,75,000
Credit Revenue from Operations	2,70,000
Credit Purchases	1,80,000
Average Trade Receivables	30,000
Average Trade Payables	16,000
Cost of Revenue from Operations	2,16,000
Operating Expenses	24,000

(I.S.C. 2009)

[**Ans.** (*i*) Debt equity ratio .5 : 1; (*ii*) Debt to Total assets ratio .14 : 1; (*iii*) Operating ratio 88.89%; (*iv*) Trade Receivables turnover ratio 9 times; (*v*) Trade Payables turnover ratio 11.25 times.]

Q. 168. From the following information, calculate :

(*a*) Liquid Ratio (*b*) Working Capital Turnover Ratio
(*c*) Operating Ratio (*d*) Net Profit Ratio

Give the answer up to two decimal places.

Cost of Revenue from Operations	6,00,000
Operating Expenses	50,000
Revenue from Operations	8,00,000
Revenue from Operations Returns	10,000
Total Current Assets	3,00,000
Total Current Liabilities	1,00,000
Total Assets	7,00,000
Closing Inventory	30,000
Prepaid Insurance	5,000

(From I.S.C. Guidelines, 2013)

SOLUTION :

(*a*) Liquid Ratio $= \dfrac{\text{Quick Assets}}{\text{Current Liabilities}}$

$$= \frac{3{,}00{,}000 - 30{,}000 - 5{,}000}{1{,}00{,}000} = \frac{2{,}65{,}000}{1{,}00{,}000} = 2.65 : 1$$

(*b*) Working Capital Turnover Ratio $= \dfrac{\text{Revenue from Operations}}{\text{Working Capital}}$

$$= \frac{8{,}00{,}000 - 10{,}000}{3{,}00{,}000 - 1{,}00{,}000}$$

$$= \frac{7{,}90{,}000}{2{,}00{,}000} = 3.95 \text{ times}$$

(*c*) Operating Ratio

$$= \frac{\text{Cost of Revenue from Operations} + \text{Operating Expenses}}{\text{Net Revenue from Operations}} \times 100$$

$$= \frac{6{,}00{,}000 + 50{,}000}{8{,}00{,}000 - 10{,}000} \times 100 = \frac{6{,}50{,}000}{7{,}90{,}000} \times 100 = 82.28\%$$

(*d*) Net Profit Ratio $= \dfrac{\text{Net Profit}}{\text{Net Revenue from Operations}} \times 100$

$$= \frac{\text{Gross Profit} - \text{Operating Expenses}}{\text{Net Revenue from Operations}} \times 100$$

$$= \frac{1{,}90{,}000^{*} - 50{,}000}{7{,}90{,}000} \times 100 = 17.72\%$$

*Gross Profit = Revenue from Operations – Revenue from Operations Returns – Cost of Revenue from Operations
= ₹8,00,000 – ₹10,000 – ₹6,00,000 = ₹1,90,000

Q. 169. (*i*) How will you assess the liquidity of a business?

(*ii*) Calculate Gross Profit Ratio from the following information :

Cash Revenue from Operations is 1/4th of the total Revenue from Operations
Cash Revenue from Operations were ₹8,00,000.
Credit Purchases are 1/5th of the total purchases.
Credit Purchases were ₹3,00,000.
Opening Inventory ₹1,00,000. Closing Inventory was ₹40,000 more than the Opening Inventory.
Wages ₹30,000
Carriage outward ₹16,000. *(From I.S.C. Guidelines, 2013)*

SOLUTION.

(*i*) The liquidity of a business is assessed by calculating its Current Ratio and Liquid Ratio.

(*ii*) Cash Revenue = 1/4th of the total revenue from operations = 8,00,000
So Total Revenue from Operations = 8,00,000 × 4 = 32,00,000
Credit Purchases = 1/5th of the total purchases = 3,00,000
So Total Purchases = 3,00,000 × 5 = 15,00,000
Cost of Revenue from Operations = Net Purchases + Direct Expenses (Wages) + Change in Inventory
= 15,00,000 + 30,000 – 40,000
= 14,90,000

Gross Profit = Revenue from Operations – Cost of Revenue from Operations
= 32,00,000 – 14,90,000 = 17,10,000

$$\text{Gross Profit Ratio} = \frac{\text{Gross Profit}}{\text{Net Revenue from Operations}} \times 100$$

$$= \frac{17{,}10{,}000}{32{,}00{,}000} \times 100 = 53.44\%$$

Q. 170. The following data is available from the records of Johnson and Company Limited :

Particulars	₹
Stock	50,000
Sundry debtors	40,000
Bills receivable	10,000
Advances paid	4,000
Cash in hand	30,000
Sundry creditors	60,000
Bills payable	40,000
Bank overdraft	4,000
Reserves	70,000
10% Preference Share Capital	5,00,000
Equity Share Capital	7,00,000
Net profit after tax	1,40,000

Calculate the following (up to two decimal places) :

(*i*) Current Ratio (*ii*) Quick Ratio (*iii*) Earning Per Share *(I.S.C. 2013)*

[Ans. (*i*) Current Ratio 1.29 : 1;
(*ii*) Quick Ratio 0.77 : 1
(*iii*) Earning Per Share 1.29

It is important to note that marks will be deducted if in case of Current Ratio 1.29 is written in place of 1.29 : 1 and in case of Quick Ratio 0.77 is written in place of 0.77 :1.]

Q. 171. From the following information, calculate Trade Receivables Turnover Ratio :

	₹
Credit Revenue from Operations	9,60,000
Gross Debtors	1,90,000
Bills Receivable	50,000
Provision for Doubtful Debts	10,000

(I.S.C. 2014)

[**Ans.** Trade Receivables Turnover Ratio : 4 times.]

Hint : Provision for Doubtful Debts is not deducted from Trade Receivables for the calculation of this ratio.

Q. 172. From the following information, calculate (upto two decimal places) :

(*i*) Gross Profit Ratio
(*ii*) Operating Ratio

	₹
Net Revenue from Operations	14,00,000
Credit Revenue from Operations	10,00,000
Gross Profit	5,00,000
Depreciation on fixed assets	40,000
Profit on Sale of Land	10,000
Selling Expenses	60,000

(I.S.C. Sample Question Paper 2015)

[**Ans.** (*i*) Gross Profit Ratio 35.71%; (*ii*) Operating Ratio 71.43%]

Q. 173. From the following information calculate (up to two decimal places) :

(*i*) Gross Profit Ratio
(*ii*) Inventory Turnover Ratio
(*iii*) Net Profit Ratio

	₹
Cash Revenue from Operations	70,000
Net Purchases	2,97,000
Credit Revenue from Operations	2,80,000
Closing Inventory	80,000
Opening Inventory	60,000
Carriage Inward	3,000
Selling Expenses	5,000
Administrative Expenses	40,000
Loss on Sale of Fixed Asset	10,000
Dividend Received	7,000

(ISC, 2015)

[**Ans.** (*i*) Gross Profit Ratio 20%; (*ii*) Inventory Turnover Ratio 4 times; and (*iii*) Net Profit Ratio 6.29%.]

Q. 174. Calculate 'Return on Investment' and 'Debt to Equity Ratio' from the following information :

Net Profit after Interest and Tax	₹ 6,00,000
6% Debentures	₹ 10,00,000
Tax Rate	40%
Capital Employed	₹ 20,00,000

(C.B.S.E. 2020, Kolkata, Lucknow)

SOLUTION :

(*i*) Return on Investment $= \dfrac{\text{Net Profit before Interest and Tax}}{\text{Capital Employed}} \times 100$

Calculation of Net Profit before Interest and Tax :

Net Profit after Tax $= ₹6{,}00{,}000$

Net Profit before Tax $= 6{,}00{,}000 \times \dfrac{100}{60} = ₹10{,}00{,}000$

Net Profit before Interest and Tax $= ₹10{,}00{,}000 + \text{Interest } ₹60{,}000$

$= ₹10{,}60{,}000$

Return on Investment $= \dfrac{10{,}60{,}000}{20{,}00{,}000} \times 100 = 53\%$

(*ii*) Debt Equity Ratio $= \dfrac{\text{Debt}}{\text{Equity}}$

Debt $= 6\%$ Debentures $= ₹10{,}00{,}000$

Equity $=$ Capital Employed – Debt

$= 20{,}00{,}000 - 10{,}00{,}000 = ₹10{,}00{,}000$

Debt Equity Ratio $= \dfrac{10{,}00{,}000}{10{,}00{,}000} = 1 : 1$

Q. 175. Calculate the Current Ratio and Debt-Equity Ratio from the following information :

	₹
Non-Current Assets	16,00,000
Current Assets	4,00,000
Working Capital	2,00,000
Non-Current Liabilities	12,00,000

(C.B.S.E. 2020, Rajasthan)

SOLUTION :

(*i*) **Calculation of Current Ratio :**

Current Liabilities $=$ Current Assets – Working Capital

$= ₹4{,}00{,}000 - ₹2{,}00{,}000 = ₹2{,}00{,}000$

Current Ratio $= \dfrac{\text{Current Assets}}{\text{Current Liabilities}} = \dfrac{4{,}00{,}000}{2{,}00{,}000} = 2 : 1$

(ii) Calculation of Debt-equity Ratio :

Debts = Non Current Liabilities *i.e.* ₹12,00,000

Equity = Non Current Assets + Working Capital – Non Current Liabilities
= ₹16,00,000 + ₹2,00,000 – ₹12,00,000
= ₹6,00,000

Debt Equity Ratio = $\frac{\text{Debt}}{\text{Equity}} = \frac{₹12,00,000}{₹6,00,000} = 2 : 1$

Q. 176. From the following information obtained from the books of Kamal Ltd., Calculate (*i*) Gross Profit Ratio and (*ii*) Net Profit Ratio.

	(₹)
Revenue from Operations	2,50,000
Purchases	1,05,000
Carriage Inwards	4,000
Salaries	30,000
Decrease in Inventory	15,000
Return Outwards	5,000
Wages	18,000

(C.B.S.E. 2020, Punjab)

SOLUTION

(*i*) Gross Profit Ratio = $\frac{\text{Gross Profit}}{\text{Revenue from Operations}} \times 100$

Gross Profit = Revenue from Operations – Cost of Revenue from Operations

Cost of Revenue From Operations = Purchases – Return Outwards + (Opening Inventory – Closing Inventory) + Carriage Inwards + Wages
= Purchases – Return Outwards + Decrease in Inventory + Carriage Inwards + Wages
= 1,05,000 – 5,000 + 15,000 + 4,000 + 18,000
= ₹1,37,000

Gross Profit = ₹2,50,000 – ₹1,37,000 = ₹1,13,000

Gross Profit Ratio = $\frac{₹ 1,13,000}{₹ 2,50,000} \times 100 = 45.2\%$

(*ii*) Net Profit Ratio = $\frac{\text{Net Profit}}{\text{Revenue from Operations}} \times 100$

Net Profit = Gross Profit – Salaries
= ₹1,13,000 – ₹30,000
= ₹83,000

Net Profit Ratio = $\frac{₹ 83,000}{₹ 2,50,000} \times 100 = 33.2\%$

Multiple Choice Questions

Choose the best Option :

(A) Liquidity Ratios

Q. 1. Two basic measures of liquidity are :

(A) Inventory turnover and Current ratio
(B) Current ratio and Quick ratio
(C) Gross Profit ratio and Operating ratio
(D) Current ratio and Average Collection period

Q. 2. Current Ratio is :

(A) Solvency Ratio
(B) Liquidity Ratio
(C) Activity Ratio
(D) Profitability Ratio

Q. 3. Current Ratio is :

(A) Liquid Assets/Current Assets
(B) Fixed Assets/Current Assets
(C) Current Assets/Current Liabilities
(D) Liquid Assets/Current Liabilities

Q. 4. Liquid Assets do not include :

(A) Bills Receivable
(B) Debtors
(C) Inventory
(D) Bank Balance

Q. 5. Ideal Current Ratio is :

(A) 1 : 1
(B) 1 : 2
(C) 1 : 3
(D) 2 : 1

Q. 6. Working Capital is the :

(A) Cash and Bank Balance
(B) Capital borrowed from the Banks
(C) Difference between Current Assets and Current Liabilities
(D) Difference between Current Assets and Fixed Assets

Q. 7. Current assets include only those assets which are expected to be realised within ....

(A) 3 months
(B) 6 months
(C) 1 year
(D) 2 years

Q. 8. The .... of a business firm is measured by its ability to satisfy its short term obligations as they become due.

(A) Activity
(B) Liquidity
(C) Debt
(D) Profitability

Q. 9. Ideal Quick Ratio is :

(A) 1 : 1
(B) 1 : 2
(C) 1 : 3
(D) 2 : 1

Q. 10. Quick Assets do not include

(A) Cash in Hand
(B) Prepaid Expenses
(C) Marketable Securities
(D) Trade Receivables

11. Current Assets do not include :

(A) Prepaid Expenses
(B) Inventory
(C) Goodwill
(D) Bills Receivable

12. Quick Ratio is also known as :

(A) Liquid Ratio
(B) Current Ratio
(C) Working Capital Ratio
(D) None of the Above

13. Liquid Assets include :

(A) Debtors
(B) Bills Receivable
(C) Bank Balance
(D) All of the Above

14. Liquid Ratio is equal to liquid assets divided by :

(A) Non-Current Liabilities
(B) Current Liabilities
(C) Total Liabilities
(D) Contingent Liabilities

15. Patents and Copyrights fall under the category of :

(A) Current Assets
(B) Liquid Assets
(C) Intangible Assets
(D) None of Above

16. Cash Balance ₹15,000; Trade Receivables ₹35,000; Inventory ₹40,000; Trade Payables ₹24,000 and Bank Overdraft is ₹6,000. Current Ratio will be :

(A) 3.75 : 1
(B) 3 : 1
(C) 1 : 3
(D) 1 : 3.75

17. Trade Receivables ₹40,000; Trade Payables ₹60,000; Prepaid Expenses ₹10,000; Inventory ₹1.00.000 and Goodwill is ₹15,000. Current Ratio will be :

(A) 1 : 2
(B) 2 : 1
(C) 2.33 : 1
(D) 2.5 : 1

18. Cash Balance ₹5,000; Trade Payables ₹40,000; Inventory ₹50,000; Trade Receivables ₹65.000 and Prepaid Expenses are ₹10.000. Liquid Ratio will be :

(A) 1.75 : 1
(B) 2 : 1
(C) 3.25 : 1
(D) 3 : 1

19. Current Assets ₹4.00.000; Current Liabilities ₹2.00.000 and Inventory is ₹50,000. Liquid Ratio will be :

(A) 2 : 1
(B) 2.25 : 1
(C) 4 : 7
(D) 1.75 : 1

20. Which of the following transactions will improve the Current Ratio :

(A) Cash Collected from Trade Receivables
(B) Purchase of goods for cash
(C) Payment to Trade Payables
(D) Credit purchase of Goods

21. Which of the following transactions will improve the quick ratio?

(A) Sale of goods for cash
(B) Sale of goods on credit
(C) Issue of new shares for cash
(D) All of the Above

Q. 22. A company's Current Ratio is 2 : 1. After cash payment to some of its creditors, Current Ratio will :

(A) Decrease
(B) Increase
(C) As before
(D) None of these

Q. 23. A Company's Current Assets are ₹8,00,000 and its current liabilities are ₹4,00,000. Subsequently, it purchased goods for ₹1,00,000 on credit. Current ratio will be ……………

(A) 2 : 1
(B) 2.25 : 1
(C) 1.8 : 1
(D) 1.6 : 1

Q. 24. A company's Current assets are ₹3,00,000 and its current liabilities are ₹2,00,000. Subsequently, it paid ₹50,000 to its trade payables. Current ratio will be ……………

(A) 2 : 1
(B) 1.67 : 1
(C) 1.25 : 1
(D) 1.5 : 1

Q. 25. Current Assets of a Company were ₹1,00,000 and its current ratio was 2 : 1. After this the company paid ₹25,000 to a Trade Payable. The Current Ratio after the payment will be

(A) 5 : 1
(B) 2 : 1
(C) 3 : 1
(D) 4 : 1

Q. 26. Current liabilities of a company were ₹2,00,000 and its current ratio was 2.5 : 1. After this the company paid ₹1,00,000 to a trade payable. The current ratio after the payment will be :

(A) 2 : 1
(B) 4 : 1
(C) 5 : 1
(D) None of the above

Q. 27. A Company's liquid assets are ₹10,00,000 and its current liabilities are ₹8,00,000. Subsequently, it purchased goods for ₹1,00,000 on credit. Quick ratio will be ……………

(A) 1.11 : 1
(B) 1.22 : 1
(C) 1.38 : 1
(D) 1.25 : 1

Q. 28. A Company's liquid assets are ₹5,00,000 and its current liabilities are ₹3,00,000. Thereafter, it paid ₹1,00,000 to its trade payables. Quick ratio will be:

(A) 1.33 : 1
(B) 2.5 : 1
(C) 1.67 : 1
(D) 2 : 1

Q. 29. The ……………… is a measure of liquidity which excludes ……………, generally the least liquid asset

(A) Current ratio, Accounts receivable

(B) Liquid ratio, Accounts receivable

(C) Current ratio, inventory

(D) Liquid ratio, inventory

Q. 30. Assuming that the current ratio is 2 : 1, purchase of goods on credit would

(A) Increase Current ratio
(B) Decrease Current ratio
(C) have no effect on Current ratio
(D) decrease gross profit ratio

Q. 31. Assuming that the current ratio is 2 : 1, Cash paid against Bills Payable would:
(A) increase current ratio
(B) Decrease Current ratio
(C) have no effect on Current ratio
(D) decrease gross profit ratio

Q. 32 Assuming liquid ratio of 1.2 : 1, cash collected from debtors would :
(A) increase liquid ratio
(B) decrease liquid ratio
(C) have no effect on liquid ratio
(D) increase gross profit ratio

Q. 33. Liquid Assets :
(A) Current Assets – Prepaid Exp.
(B) Current Assets – Inventory + Prepaid Exp.
(C) Current Assets – Inventory – Prepaid Exp.
(D) Current Assets + Inventory – Prepaid Exp.

Q. 34 Current Assets ₹85,000; Inventory ₹22,000; Prepaid Expenses ₹3,000. Then liquid assets will be :
(A) ₹63,000
(B) ₹ 60,000
(C) ₹82,000
(D) ₹1,10,000

Q. 35 A Company's Quick Ratio is 1.5 : 1; Current Liabilities are ₹2,00,000 and Inventory is ₹1,80,000. Current Ratio will be :
(A) 0.9 : 1
(B) 1.9 : 1
(C) 1.4 : 1
(D) 2.4 : 1

Q. 36. A Company's Quick Ratio is 1.8 : 1; Liquid Assets are ₹5,40,000 and Inventory is ₹1,50,000. Its Current Ratio will be :
(A) 2 : 1
(B) 2.3 : 1
(C) 1.8 : 1
(D) 1.3 : 1

Q. 37. A Company's Current Ratio is 2.8 : 1; Current Liabilities are ₹2,00,000; Inventory is ₹1,50,000 and Prepaid Expenses are ₹10,000. Its Liquid Ratio will be :
(A) 3.6 : 1
(B) 2.1 : 1
(C) 2 : 1
(D) 2.05 : 1

Q. 38. A Company's Current Ratio is 3 : 1; Current Liabilities are ₹2,50,000; Inventory is ₹60,000 and Prepaid Expenses are ₹5,000. Its Liquid Assets will be :
(A) ₹6,90,000
(B) ₹6,95,000
(C) ₹6,85,000
(D) ₹8,15,000

Q. 39. On the basis of following data, the liquid ratio of a company will be : Curren Ratio 5 : 3; Current Liabilities ₹75,000 and Inventory ₹25,000
(A) 1 : 1
(B) 2 : 1.8
(C) 3 : 2
(D) 4 : 3

Q. 40. Current ratio of a firm is 9 : 4. Its current liabilities are ₹1,20,000. Inventor is ₹30,000. Its liquid ratio will be :
(A) 1 : 1
(B) 1.5 : 1
(C) 2 : 1
(D) 1.6 : 1

Q. 41. A firm's current ratio is 3.5 : 2. Its current liabilities are ₹80,000. Its working capital will be :

(A) ₹1,20,000
(B) ₹1,60,000
(C) ₹ 60,000
(D) ₹2,80,000

Q. 42. A Company's Current Ratio is 3 : 1 and Liquid Ratio is 1.2 : 1. If its Current Liabilities are ₹2,00,000, what will be the value of Inventory?

(A) ₹2,40,000
(B) ₹3,60,000
(C) ₹4,00,000
(D) ₹ 40,000

Q. 43. A Company's Current Ratio is 2.5 : 1 and Liquid Ratio is 1.6 : 1. If its Current Assets are ₹7,50,000, what will be the value of Inventory?

(A) ₹4,50,000
(B) ₹4,80,000
(C) ₹2,70,000
(D) ₹1,80,000

Q. 44. Current Ratio of a Company is 2.5 : 1. If its working capital is ₹60,000, its current liabilities will be :

(A) ₹ 40,000
(B) ₹60,000
(C) ₹1,00,000
(D) ₹24,000

Q. 45. A Company's Current Assets are ₹6,00,000 and working capital is ₹2,00,000. Its Current Ratio will be :

(A) 3 : 1
(B) 1.5 : 1
(C) 2 : 1
(D) 4 : 1

Q. 46. A Company's Current Ratio is 2.4 : 1 and Working Capital is ₹5,60,000. If its Liquid Ratio is 1.5, what will be the value of Inventory?

(A) ₹6,00,000
(B) ₹2,00,000
(C) ₹3,60,000
(D) ₹6,40,000

Q. 47. A Company's Current Ratio is 2.5 : 1 and its Working Capital is ₹60,000. If its Inventory is ₹52,000, what will be the liquid Ratio?

(A) 2.3 : 1
(B) 2.8 : 1
(C) 1.3 : 1
(D) 1.2 : 1

Q. 48. If a Company's Current Liabilities are ₹80,000; Working Capital is ₹2,40,000 and Inventory is ₹40,000, its quick ratio will be:

(A) 3.5 : 1
(B) 4 : 1
(C) 4.5 : 1
(D) 3 : 1

Q. 49. A Company's Liquid Assets are ₹2,00,000, Inventory is ₹1,00,000, Prepaid Expenses are ₹20,000 and Working Capital is ₹2,40,000. Its Current Ratio will be:

(A) 1.33 : 1
(B) 4 : 1
(C) 2.5 : 1
(D) 3 : 1

Q. 50. The Current Ratio of a company is 1.8:1 and its Quick Ratio is 1.6 : 1.

From the following transactions, pick out the transaction which involves an increase in both the Current Ratio and Quick Ratio:

(A) Goods worth ₹10,000 sold at a loss of ₹2,000.
(B) Insurance premium of ₹3,000 paid in advance.
(C) Plant and Machinery purchased for ₹9,000.
(D) Bills Payable of ₹2,000 honoured on the due date.

(I.S.C. Sample Paper, 2021)

Q. 51. Which ratio indicates the proportion of assets financed out of shareholders' funds?

(A) Debt equity ratio.
(B) Fixed assets turnover ratio.
(C) Proprietary ratio.
(D) Total assets to debt ratio.

(C.B.S.E. Sample Paper, 2021)

3) Solvency Ratios

Q. 52. Long term solvency is indicated by :

(A) Current Ratio
(B) Quick Ratio
(C) Net Profit Ratio
(D) Debt/Equity Ratio

Q. 53. Debt Equity Ratio is :

(A) Liquidity Ratio
(B) Solvency Ratio
(C) Activity Ratio
(D) Operating Ratio

Q. 54. Debt Equity Ratio is :

(A) Long Term Debts/Shareholder's Funds
(B) Short Term Debts/Equity Capital
(C) Total Assets/Long term Debts
(D) Shareholder's Funds/Total Assets

Q. 55. Proprietary Ratio is :

(A) Long term Debts/Shareholder's Funds
(B) Total Assets/Shareholder's Funds
(C) Shareholder's Funds/Total Assets
(D) Shareholder's Funds/Fixed Assets

Q. 56. Fixed Assets ₹5,00,000; Current Assets ₹3,00,000; Equity Share Capital ₹4,00,000; Reserve ₹2,00,000; Long-term Debts ₹40,000. Proprietary Ratio will be :

(A) 75%
(B) 80%
(C) 125%
(D) 133%

Q. 57. The .... ratios provide the information critical to the long run operation of the firm.

(A) Liquidity
(B) Activity
(C) Solvency
(D) Profitability

Q. 58. If Debt equity ratio exceeds ...., it indicates risky financial position.

(A) 1 : 1
(B) 2 : 1
(C) 1 : 2
(D) 3 : 1

Q. 59. In debt equity ratio, debt refers to :

(A) Short Term Debts
(B) Long Term Debts
(C) Total Debts
(D) Debentures and Current Liabilities

Q. 60. Proprietary Ratio indicates the relationship between Proprietor's Funds and ....

(A) Long-Term Debts
(B) Short Term & Long Term Debts
(C) Total Assets
(D) Debentures

Q. 61. The formula for calculating the Debt Equity Ratio is :

(A) $\frac{\text{Short Term Debts}}{\text{Shareholder's Funds}}$

(B) $\frac{\text{Shareholder's Funds}}{\text{Fixed Assets}}$

(C) $\frac{\text{Short Term + Long Term Debts}}{\text{Shareholder's Funds}}$

(D) None of the Above

Q. 62. Equity Share Capital ₹20,00,000, Reserve 5,00,000; Debentures ₹10,00,000, Current Liabilities ₹8,00,000. Debt-equity ratio will be

(A) 4 : 1

(B) .32 : 1

(C) .72 : 1

(D) [illegible] : 1

Q. 63. Debt equity ratio of a company is 1 : 2. Which of the following transactions will increase it

(A) Issue of new shares for cash

(B) Redemption of Debentures

(C) Issue of Debentures for cash

(D) Goods purchased on credit

Q. 64. Satisfactory ratio between Long-term Debts and Shareholder's Funds is

(A) 1 : 1

(B) 3 : 1

(C) 1 : 2

(D) 2 : 1

Q. 65. On the basis of following data, the Debt-Equity Ratio of a Company will be:
Equity Share Capital ₹5,00,000; General Reserve ₹3,20,000; Preliminary Expenses ₹20,000; Debentures ₹1,20,000; Current Liabilities ₹80,000

(A) 1 : 2

(B) .32 : 1

(C) 4 : 1

(D) .31 : 1

Q. 66 On the basis of following information received from a firm, its Debt-Equity Ratio will be:
Equity Share Capital ₹5,50,000; Reserve Fund ₹4,30,000; Preliminary Expenses ₹40,000; Long term Debts ₹1,28,900; Debentures ₹2,30,000

(A) .42 : 1

(B) .33 : 1

(C) .43 : 1

(D) .37 : 1

Q. 67. On the basis of following data, the proprietary ratio of a Company will be:
Equity Share Capital ₹6,00,000, Debentures ₹2,40,000, Statement of Profit & Loss Debit Balance ₹40,000

(A) 74%

(B) 68%

(C) 82%

(D) 70%

Q. 68. On the basis of following information received from a firm, its Proprietary Ratio will be :
Fixed Assets ₹3,30,000; Current Assets ₹1,90,000; Preliminary Expenses ₹30,000; Equity Share Capital ₹2,44,000; Preference Share Capital ₹1,70,000; Reserve Fund ₹58,000

(A) 70%

(B) 80%

(C) 85%

(D) 90%

Q. 69. On the basis of following data, a Company's Total Assets-Debt Ratio will be:
Working Capital ₹4,50,000; Current Liabilities ₹1,50,000; Fixed Assets

₹4,00,000; Debentures ₹2,00,000; Long Term Bank Loan ₹50,000.

(A) 5 : 1 (B) 4 : 1
(C) 2.5 : 1 (D) 20 : 1

Hint : Working Capital + Current Liabilities = Current Assets

Q. 70. On the basis of following information received from a firm, its Total Assets-Debt Ratio will be :
Shareholder's Funds ₹2,00,000; Dr. Balance of Profit & Loss ₹50,000; Current Liabilities ₹1,00,000; Current Assets ₹2,00,000; Total Assets ₹6,00,000.

(A) 2 : 1 (B) 1.5 : 1
(C) 3 : 1 (D) 1.71 : 1

(C) Activity Ratios

Q. 71. Inventory Turnover Ratio is :

(A) Average Inventory/Revenue from Operations
(B) Average Inventory/Cost of Revenue from Operations
(C) Cost of Revenue from Operations/Average Inventory
(D) G.P./Average Inventory

Q. 72. Opening Inventory ₹1,00,000; Closing Inventory ₹1,50,000; Purchases ₹6,00,000; Carriage ₹25,000; Wages ₹2,00,000. Inventory Turnover Ratio will be :

(A) 6.6 Times (B) 7.4 Times
(C) 7 Times (D) 6.2 Times

Q. 73. Revenue from Operations ₹8,00,000; Gross Profit Ratio 25%; Opening Inventory ₹1,00,000; Closing Inventory ₹60,000. Inventory Turnover Ratio will be :

(A) 10 Times (B) 7.5 Times
(C) 8 Times (D) 12.5 Times

Q. 74. On the basis of following data, the cost of revenue from operations by a company will be :
Opening Inventory ₹70,000; Closing Inventory ₹80,000; Inventory Turnover Ratio 6 Times.

(A) ₹1,50,000 (B) ₹ 90,000
(C) ₹4,50,000 (D) ₹4,80,000

Q. 75. Opening Inventory of a firm is ₹80,000. Cost of revenue from operations is ₹6,00,000. Inventory Turnover Ratio is 5 times. Its closing Inventory will be:

(A) ₹1,60,000 (B) ₹1,20,000
(C) ₹ 80,000 (D) ₹2,00,000

Q. 76. Cost of revenue from operations ₹6,00,000; Inventory Turnover Ratio 5; Find out the value of opening inventory, if opening inventory is ₹8,000 less than the closing inventory.

(A) ₹1,12,000 (B) ₹1,16,000
(C) ₹1,28,000 (D) ₹1,24,000

Q. 77. Revenue from Operations ₹2,00,000; Inventory Turnover Ratio 5; Gross Profit 25%. Find out the value of Closing Inventory, if Closing Inventory is ₹8,000 more than the Opening Inventory.

(A) ₹38,000 (B) ₹22,000

(C) ₹34,000 (D) ₹26,000

Q. 78. If the inventory turnover ratio is divided into 365, it becomes a measure of ....

(A) Sales efficiency (B) Average Age of Inventory

(C) Sales Turnover (D) Average Collection Period

Q. 79. If average inventory is ₹50,000 and closing inventory is ₹2,000 less than the opening inventory, opening and closing inventory will be :

(A) ₹52,000 and ₹50,000 (B) ₹50,000 and ₹48,000

(C) ₹48,000 and ₹46,000 (D) ₹51,000 and ₹49,000

Q. 80. Opening Inventory ₹50,000; Closing Inventory ₹40,000 and cost of revenue from operations ₹7,20,000. What will be Inventory Turnover Ratio?

(A) 18 Times (B) 16 Times

(C) 14.4 Times (D) 8 Times

Q. 81. Average Inventory ₹60,000; Inventory Turnover Ratio 8; Gross Profit 20% on revenue from operations; what will be Gross Profit?

(A) ₹1,20,000 (B) ₹96,000

(C) ₹ 80,000 (D) ₹15,000

Q. 82. Opening Inventory ₹75,000; Closing Inventory ₹1,05,000; Inventory Turnover Ratio 6; Gross Profit 20% on cost; what will be Gross Profit?

(A) ₹1,35,000 (B) ₹1,08,000

(C) ₹ 90,000 (D) ₹ 18,000

Q. 83. What will be the amount of gross profit of a firm if its average inventory is ₹80,000, Inventory turnover ratio is 6 times, and the Selling price is 25% above cost?

(A) ₹1,20,000. (B) 1,60,000.

(C) ₹2,00,000. (D) None of the above.

(C.B.S.E. Sample Paper, 2021)

Q. 84. Opening Inventory ₹40,000; Purchase ₹4,00,000; Purchase Return ₹12,000, what will be Inventory turnover ratio if Closing Inventory is less than Opening Inventory by ₹8,000?

(A) 9 Times (B) 10.78 Times

(C) 11 Times (D) 8.82 Times

Q. 85. The formula for calculating the Trade Receivables Turnover Ratio is :

(A) $\dfrac{\text{Total Revenue from Operations}}{\text{Average Debtors}}$

(B) $\dfrac{\text{Credit Revenue from Operations}}{\text{Average Debtors}}$

(C) $\dfrac{\text{Net Credit Revenue from Operations}}{\text{Average Debtors + Average Bills Receivable}}$

(D) None of the Above

Q. 86. Total revenue from operations ₹9,00,000; Cash revenue from operations ₹3,00,000; Debtors ₹1,00,000; B/R ₹20,000. Trade Receivables Turnover Ratio will be :

(A) 5 Times (B) 6 Times

(C) 7.5 Times (D) 9 Times

Q. 87. Total revenue from operations ₹27,00,000; Credit revenue from operations ₹18,00,000; Opening Debtors ₹3,20,000; Closing Debtors ₹4,00,000; Provision for Doubtful Debts ₹60,000. Trade Receivables Turnover Ratio will be :

(A) 7.5 times (B) 9 times

(C) 6 times (D) 5 times

Q. 88. If Total sales is ₹2,50,000 and credit sales is 25% of Cash sales. The amount of credit sales is :

(A) ₹50,000 (B) ₹2,50,000

(C) ₹16,000 (D) ₹3,00,000

(C.B.S.E. Sample Paper, 2021)

Q. 89. From the given particulars of Zee Ltd., the Trade Receivables Turnover Ratio of the company will be:

Particulars	₹
Revenue from Operations	12,00,000
Cash Revenue from Operations	25% of Credit Revenue from Operations
Gross Debtors	1,90,000
Bills Receivable	50,000
rovision for Doubtful Debts	10,000

(A) 3.75 times (B) 4 times

(C) 4.17 times (D) 8 times

(I.S.C. Sample Paper, 2021)

Q. 90. Credit revenue from operations ₹24,00,000; Trade Receivables Turnover Ratio 6 times; Opening Debtors ₹3,20,000. Closing Debtors will be :

(A) ₹4,00,000 (B) ₹4,80,000

(C) ₹ 80,000 (D) ₹7,20,000

Q. 91. A firm makes credit revenue from operations of ₹2,40,000 during the year. If the trade receivables turnover ratio is 8 times, calculate closing debtors, if the closing debtors are more by ₹6,000 than the opening debtors :

(A) ₹33,000 (B) ₹36,000

(C) ₹24,000 (D) ₹27,000

Q. 92. Credit revenue from operations ₹3,00,000. Trade Receivables Turnover Ratio 5; Calculate Closing Debtors, if closing debtors are two times in comparison to Opening Debtors.

(A) ₹40,000 (B) ₹ 60,000

(C) ₹80,000 (D) ₹1,20,000

Q. 93. Credit revenue from operations ₹5,60,000; Debtors ₹70,000; B/R ₹10,000. Average Collection Period will be :

(A) 52 Days (B) 53 Days

(C) 45 Days (D) 46 Days

Q. 94. Credit revenue from operations ₹6,00,000; Cash revenue from operations ₹1,50,000, Debtors ₹1,00,000; B/R ₹50,000. Average Collection Period will be :

(A) 2 Months (B) 2.4 Months

(C) 3 Months (D) 1.6 Months

Q. 95. On the basis of following data, a Company's closing debtors will be: Credit revenue from operations ₹9,00,000; Average Collection period 2 months; Opening debtors are ₹15,000 less as compared to closing debtors.

(A) ₹1,42,500 (B) ₹1,57,500

(C) ₹1,80,000 (D) ₹ 75,000

Q. 96. Total credit revenue from operations of a firm is ₹5,40,000. Average collection period is 3 months. Opening debtors are ₹1,10,000. Its closing debtors will be :

(A) ₹1,35,000 (B) ₹1,60,000

(C) ₹2,20,000 (D) ₹1,80,000

Q. 97. The formula for calculating Trade Payables Turnover Ratio is :

(A) $\frac{\text{Net Credit Purchases}}{\text{Average Creditors}}$

(B) $\frac{\text{Net Credit Purchases}}{\text{Average Creditors + Average Bills Payable}}$

(C) $\frac{\text{Cash Purchases}}{\text{Total Creditors}}$

(D) None of the Above

Q. 98. Credit Purchases ₹12,00,000; Opening Creditors ₹2,00,000; Closing Creditors ₹1,00,000. Trade Payables Turnover Ratio will be :

(A) 6 times (B) 4 times

(C) 8 times (D) 12 times

Q. 99. Total Purchases ₹4,50,000; Cash Purchases ₹1,50,000; Creditors ₹50,000; Bills Payable ₹10,000. Trade Payables Turnover Ratio will be :

(A) 7.5 times (B) 6 times

(C) 9 times (D) 5 times

Q. 100. Credit Purchases ₹6,00,000; Trade Payables Turnover Ratio 5; Calculate closing creditors, if closing creditors are ₹10,000 less than opening creditors.

(A) ₹1,15,000 (B) ₹1,25,000

(C) ₹1,30,000 (D) ₹1,10,000

Q. 101 Credit Purchases ₹9,60,000; Cash Purchases ₹6,40,000; Creditors ₹2,40,000; Bills Payable ₹80,000. Average Payment Period will be :

(A) 3 months
(B) 4 months
(C) 2.4 months
(D) 6 months

Q. 102. Current Assets ₹5,00,000; Current Liabilities ₹1,00,000; Revenue from Operations ₹28,00,000. Working Capital turnover Ratio will be:

(A) 7 times
(B) 5.6 times
(C) 8 times
(D) 10 times

Q. 103. On the basis of following data, the Working Capital Turnover Ratio of a company will be :
Liquid Assets ₹3,70,000; Inventory ₹80,000; Current Liabilities ₹1,50,000; Cost of revenue from operations ₹7,50,000.

(A) 2.5 Times
(B) 3 Times
(C) 5 Times
(D) 3.8 Times

Q. 104. A firm's current assets are ₹3,60,000; current ratio is 3 : 1. Cost of revenue from operations is ₹12,00,000. Its working capital turnover ratio will be :

(A) 3 Times
(B) 5 Times
(C) 8 Times
(D) 4 Times

(D) Profitability Ratios

Q. 105. Opening Inventory ₹1,00,000; Closing Inventory ₹1,20,000; Purchase ₹20,00,000; Wages ₹2,40,000; Carriage Inwards ₹1,50,000; Selling Exp ₹60,000; Revenue from Operations ₹30,00,000. Gross Profit ratio will be :

(A) 29%
(B) 26%
(C) 19%
(D) 21%

Q. 106. Cash Revenue from Operations ₹4,00,000; Credit Revenue from Operatio ₹21,00,000; Revenue from Operations Return ₹1,00,000; Cost of reven from operations ₹19,20,000. G.P. ratio will be

(A) 4%
(B) 23.2%
(C) 80%
(D) 20%

Q. 107. A firm's credit revenue from operations is ₹3,60,000, cash revenue fr operations is ₹70,000. Cost of revenue from operations is ₹3,61,200. Its gr profit ratio will be :

(A) 11%
(B) 15%
(C) 18%
(D) 16%

Q. 108. On the basis of following data, a Company's Gross Profit Ratio will be :
Net Profit ₹40,000; Office Expenses ₹20,000; Selling Expenses ₹36,
Total revenue from operations ₹6,00,000.

(A) 16%
(B) 20%
(C) 6.67%
(D) 12.5%

Q. 109. What will be the amount of Gross Profit, if revenue from operations ₹6,00,000 and Gross Profit Ratio is 20% of cost?

(A) ₹1,50,000
(B) ₹1,00,000
(C) ₹1,20,000
(D) ₹5,00,000

Q. 110. What will be the amount of Gross Profit, if revenue from operations are ₹6,00,000 and Gross Profit Ratio 20% of revenue from operations?

(A) ₹1,50,000
(B) ₹1,00,000
(C) ₹1,20,000
(D) ₹5,00,000

Q. 111. Revenue from operations is ₹1,80,000; Rate of Gross Profit is 25% on cost. What will be the Gross Profit?

(A) ₹45,000
(B) ₹36,000
(C) ₹40,000
(D) ₹60,000

Q. 112. Operating ratio is

(A) Cost of revenue from operations + Selling Expenses/Net revenue from operations
(B) Cost of production + Operating Expenses/Net revenue from operations
(C) Cost of revenue from operations + Operating Expenses/Net Revenue from Operations
(D) Cost of Production/Net revenue from operations.

Q. 113. Cost of Revenue from Operations =

(A) Revenue from Operations – Net Profit
(B) Revenue from Operations – Gross Profit
(C) Revenue from Operations – Closing Inventory
(D) Purchases – Closing Inventory

Q. 114. Total Revenue from Operations ₹15,00,000; Cost of Revenue from Operations ₹9,00,000 and Operating Expenses ₹2,25,000. Calculate operating ratio .

(A) 75%
(B) 25%
(C) 60%
(D) 15%

Q. 115. Purchases ₹7,20,000; Office Expenses ₹30,000; Selling Expenses ₹90,000; Opening Inventory ₹1,40,000; Closing Inventory ₹80,000; Revenue from Operations ₹12,00,000. Calculate operating ratio

(A) 60%
(B) 75%
(C) 70%
(D) 65%

Q. 116. Revenue from Operations ₹6,00,000; Gross Profit 20%; Office Expenses ₹30,000; Selling Expenses ₹48,000. Calculate operating ratio

(A) 80%
(B) 85%
(C) 96.33%
(D) 93%

Q. 117. Which of the following is not operating expenses?

(A) Office Expenses
(B) Selling Expenses
(C) Bad Debts
(D) Loss by Fire

Q. 118. The net revenue from operations of Gama Ltd. is ₹14,00,000.
Its Gross profit is ₹9,00,000;
Operating expenses are ₹75,000;
Commission received is ₹5,000;
Profit from sale of fixed asset is ₹10,000.
The Operating Profit Ratio of Gama Ltd. will be:

(A) 59.29%
(B) 58.92%
(C) 60%
(D) 58.93%

(I.S.C. Sample Paper, 2021)

Q. 119. Debentures ₹80,000, Trade Payables ₹1,20,000, Trade Receivables ₹90,000, Prepaid Expenses ₹10,000, Inventory ₹2,00,000 and Goodwill is ₹60,000. Current Ratio will be :

(A) 1.5 : 1
(B) 2.5 : 1
(C) 3 : 1
(D) 1.8 : 1

ther Questions :

Q. 120. The two basis measures of operational efficiency of a company are :

(A) Inventory Turnover Ratio and Working Capital Turnover Ratio
(B) Liquid Ratio and Operating Ratio
(C) Liquid Ratio and Current Ratio
(D) Gross Profit Margin and Net Profit Margin

(C.B.S.E. Sample Paper, 2019)

. 121. The area of interest for a long term lender while analyzing financial statements will be :

(A) Liquidity
(B) Activity
(C) Solvency
(D) Profitability

. 122. Net Profit ₹1,60,000; Wages ₹80,000; Office Expenses ₹30,000; Selling Expenses ₹10,000; Revenue from Operations ₹8,00,000. Gross Profit Ratio will be :

(A) 35%
(B) 25%
(C) 15%
(D) 5%

. 123. Which of the following is not an activitiy ratio?

(A) Inventory turnover ratio
(B) Interest coverage ratio
(C) Working capital turnover ratio
(D) Trade receivables turnover ratio

(C.B.S.E. 2020, Delhi)

124. The .... may indicate that the firm is experiencing stock outs and lost sales.

(A) Average payment period
(B) Inventory turnover ratio
(C) Average collection period
(D) Quick ratio

(C.B.S.E. Sample Paper, 2020)

125. Current ratio of Vidur Pvt. Ltd. is 3 : 2. Accountant wants to maintain it at 2 : 1. Following options are available :

(*i*) He can repay Bills Payable
(*ii*) He can purchase goods on credit
(*iii*) He can take short term loan

Choose the correct option :

(A) Only (*i*) is correct
(B) Only (*ii*) is correct
(C) Only (*i*) and (*iii*) are correct
(D) Only (*ii*) and (*iii*) are correct

(C.B.S.E. Sample Paper, 2020)

Q. 126. Current ratio of Adaar Ltd. is 2.5 :1. Accountant wants to maintain it at 2 :1. Following options are available :

(*i*) He can repay Bills Payable
(*ii*) He can purchase goods on credit
(*iii*) He can take short term loan

Choose the correct option.

(A) Only (*i*) is correct
(B) Only (*ii*) is correct
(C) Only (*i*) and (*iii*) are correct
(D) Only (*ii*) and (*iii*) are correct

(C.B.S.E. Sample Paper, 2021)

Q. 127. Which of the following four companies is *not* deriving the benefit of 'trading on equity'?

(A) Mars Ltd., which has a Debt-Equity Ratio of 0.49:1
(B) Venus Ltd., which has a Debt-Equity Ratio of 1.54:1
(C) Saturn Ltd., which has a Debt-Equity Ratio of 1.62:1
(D) Pluto Ltd., which has a Debt-Equity Ratio of 2.32:1

(I.S.C. Sample Paper, 2021)

Q. 128. The correct formula for computing Earning per share is:

(A) $\dfrac{\text{Net Profit after Tax}}{\text{No. of Shares}}$

(B) $\dfrac{\text{Net Profit after Tax and Preference Dividend}}{\text{No. of Shares}}$

(C) $\dfrac{\text{Net Profit after Tax and Preference Dividend}}{\text{No. of Equity Shares}}$

(D) $\dfrac{\text{Net Profit after Tax and Preference Dividend}}{\text{No. of Preference Shares}}$

(I.S.C. Sample Paper, 2021)

Q. 129. The following groups of ratios primarily measure risk :

(A) solvency, activity, and profitability
(B) liquidity, efficiency, and solvency
(C) liquidity, activity, and profitability
(D) liquidity, solvency, and profitability

(C.B.S.E. Sample Paper, 2021)

Q. 130. Which one of the following is correct?

(*i*) A ratio is an arithmetical relationship of one number to another number.
(*ii*) Liquid ratio is also known as acid test ratio.
(*iii*) Ideally accepted current ratio is 1 : 1.

(*iv*) Debt equity ratio is the relationship between outsider's funds and shareholders' funds.

In the context of the above statements, which of the following options is correct?

(A) All (*i*), (*ii*), (*iii*) and (*iv*) are correct. (B) Only (*i*), (*ii*) and (*iv*) are correct.
(C) Only (*ii*), (*iii*) and (*iv*) are correct. (D) Only (*ii*) and (*iv*) are correct.

(C.B.S.E. Sample Paper, 2021)

(See Answers at the end of the book.)

I.S.C. ANNUAL EXAMINATION QUESTION PAPER

March, 2018

ACCOUNTS

(Class XII)

(Maximum Marks : 80)

(Time allowed : Three hours)

(Candidates are allowed additional 15 minutes for only reading the paper. They must NOT start writing during this time.)

***Part I of Section A** is Compulsory.*

*Answer **any 4** Questions from **Part II of Section A** and **any two** questions from **either Section B or Section C.***

The intended marks for questions or parts of questions are given in the brackets [].

Transactions should be recorded in the answer book.

All calculations should be shown clearly.

All working, including rough work, should be done on the same page as, and adjacent to, the rest of the answer.

SECTION A

PART I (12 Marks)

Answer all questions.

Q. 1. Answer briefly each of the following questions : [6 × 2]

(*i*) Give any two differences between Revaluation Account and Realisation Account.

(*ii*) Mention whether the following Trade Payables are current liabilities or non-current liabilities.

	Operating Cycle	*Expected period of Payment*
(a)	12 months	14 months
(b)	15 months	12 months

(*iii*) What is the minimum price at which a company can reissue its forfeited shares which were originally issued at par.

(*iv*) Give the adjusting entry and closing entry for interest on loan taken by a partner from the firm, when the firm follows the Fluctuating Capital Method.

(*v*) State two reasons for a company to purchase its own debentures from the open market.

(*vi*) Give the formula for valuation of goodwill by the Capitalisation of Average Profit Method.

PART II (48 Marks)

Answer any four questions.

Q. 2. Saturn Ltd. was registered with an authorized capital of ₹12,00,000, divided into 1,20,000 equity shares of ₹10 each. It issued 40,000 equity shares to the public at a premium of ₹5 per share, payable as follows :

On application	₹6
On allotment	₹9 (including premium of ₹5)

All the shares were applied for and allotted. One shareholder holding 500 shares did not pay the allotment money and his shares were forfeited. Out of the forfeited shares, the company reissued 400 shares at ₹7 per share fully called up.

You are required to :

(*a*) Pass journal entries in the books of the company.

(*b*) Prepare :

  (*i*) Securities Premium Reserve Account.

  (*ii*) Share Capital Account. [12]

. 3. (A) On 1st April, 2013, Rayon Ltd. issued 2,000, 9% Debentures of ₹100 each at a discount of 10%, redeemable at par on 31st March, 2017. The issue was fully subscribed. To meet the provisions of the Companies Act, 2013, the Board of Directors decided to transfer ₹30,000 to Debenture Redemption Reserve on 31st March, 2014, and the balance on 31st March, 2015. On 1st April, 2016, the company made the required investment in government securities.

The investments were encashed and the debentures were redeemed on the due date.

It is the policy of the company to write off capital losses in the year in which they occur.

You are required to pass journal entries for issue and redemption of debentures (ignore interest on debentures). [8]

(B) On 1st April, 2016, Krayon Ltd. issued 8,000, 12% Debentures of ₹100 each, redeemable at par after 5 years. The issue was fully subscribed. According to the terms of issue, interest on debentures is payable annually on 31st March. Tax deducted at source is 20%.

You are required to pass journal entries for the years 2016-17, regarding issue of debentures and interest on debentures. [4]

. 4. (A) Asif and Ravi are partners in a firm, sharing profits and losses in the ratio of 3 : 2. Their fixed capitals as on 1st April, 2016, were ₹6,00,000 and ₹4,00,000 respectively.

Their partnership deed provides for the following :

(*a*) Partners are to be allowed interest on their capital @ 10% per annum.

(*b*) They are to be charged interest on drawings @ 4% per annum.

(*c*) Asif is entitled to a salary of ₹2,000 per month.

(*d*) Ravi is entitled to a commission of 5% of the correct net profit of the firm before charging such commission.

(*e*) Asif is entitled to a rent of ₹3,000 per month for the use of his premises by the firm.

The net profit of the firm for the year ended 31st March, 2017, before providing for any of the above clauses was ₹4,00,000.

Both partners withdrew ₹5,000 at the beginning of every month for the entire year.

You are required to prepare a Profit and Loss Appropriation Account for the year ended 31st March, 2017. [8]

(B) Rita, Nina and Mita are partners in a firm sharing profits and losses in the ratio of 3 : 2 : 1. Mita dies on 1st April 2017. On the date of her death, it was decided to value goodwill on the basis of two year's purchase of weighted average profits of the firm for the last three years.

The profits of the last three years and weights assigned were :

Year	*Profit (₹)*	*Weights assigned*
2014-15	30,000 (including gain from speculation ₹10,000)	1
2015-16	80,000	2
2016-17	1,00,000	3

You are required to :

(*i*) Calculate the firm's goodwill on the date of Mita's death (Show the working with the formula).

(*ii*) Pass the necessary journal entry to credit Mita's Capital Account with her share of goodwill. [4]

Q. 5. Annie and Bonnie are partners in a firm, sharing profits and losses equally. Their Balance Sheet as at 31st March, 2017 was as follows :

Balance Sheet of Annie and Bonnie
As at 31st March, 2017

Liabilities		*Amount* ₹	*Assets*		*Amount* ₹
Sundry Creditors		21,000	Cash at Bank		20,000
General Reserve		15,000	Sundry Debtors	22,000	
Capital A/c			*Less :* Provision for Doubtful Debts	(1,000)	21,000
Annie	45,000		Stock		10,000
Bonnie	40,000	85,000	Plant & Machinery		60,000
			Goodwill		10,000
		1,21,000			1,21,000

Carl was to be taken as a partner for 1/4 share in the profits of the firm, with effect from 1st April, 2017, on the following terms :

(*a*) Bad debts amounting to ₹1,500 to be written off.

(*b*) Stock to be taken over by Annie at ₹12,000.

(*c*) Plant and Machinery to be valued at ₹50,000.

(*d*) Goodwill of the firm to be valued at ₹20,000.

(*e*) Carl to bring in ₹50,000 as his capital. He was unable to bring in cash, his share of goodwill.

(*f*) General Reserve not to be distributed. For his, it was decided that Carl would compensate the old partners through his current account.

You are required to :

(*i*) Pass journal entries on the date of Carl's admission.

(*ii*) Prepare the Balance sheet of the reconstituted firm. [12]

5. (A) Harish, Paresh and Mahesh were three partners sharing profits and losses in the ratio of 5 : 4 : 1.

Paresh retired on 31st March, 2017. His capital as on 1st April, 2016 was ₹80,000. During the year 2016-17, he made drawings of ₹5,000. He was to be charged interest on drawings of ₹100.

The partnership deed provides that on the retirement of a partner, he will be entitled to :

(*i*) His share of capital.

(*ii*) Interest on capital @ 10% per annum.

(*iii*) His share of profit in the year of retirement.

(*iv*) His share of goodwill of the firm.

(*v*) His share in the profit/loss on revaluation of assets and liabilities.

Additional information :

(*a*) Paresh's share in the profits of the firm for the year 2016-17 was ₹20,000.

(*b*) Goodwill of the firm was valued at ₹24,000.

(*c*) The firm suffered a loss of ₹12,000 on the revaluation of assets and liabilities.

(*d*) It was decided to transfer the amount due to Paresh to his loan account bearing interest @ 6% per annum. The loan was to be repaid in two equal annual instalments, the first instalment to be paid on 31st March, 2018.

You are required to prepare :

(*i*) Paresh's Capital Account.

(*ii*) Paresh's Loan Account till it is finally closed. [8]

(B) Parth, Angad and Leesha are partners in a firm sharing profits and losses in the ratio of 3 : 2 : 1 respectively. Angad retired and his claim, including his Capital and entitlements from the firm including his share of Goodwill of the firm, is ₹50,000.

After this amount was determined, it was found that there was an unrecorded piece of furniture valued at ₹12,000 which had to be recorded.

Upon recording this piece of furniture, the revised amount due to Angad was determined and settled by giving him this piece of furniture and the balance in cash.

You are required to give the journal entries for recording the payment to Angad in the books of the firm. [4]

Q. 7. The following balances have been extracted from the books of Vanity Ltd. as at 31st March, 2017 :

Trial Balance as at 31st March, 2017

Particulars	Debit	Credit
	₹	₹
Equity Share Capital (5,000 shares of ₹100 each fully paid)		5,00,000
Fixed Assets	7,30,000	
Reserves and Surplus		2,00,000
Inventories	50,000	
Cash and Bank Balances	1,70,000	
Creditors		40,000
Bills Payable		20,000
Underwriting Commission on issue of shares	10,000	
5% Debentures ($\frac{1}{5}$ of Debentures to be redeemed on 31st March, 2018		2,00,000
Provision for Taxation		12,000
Interest accrued and due on 5% Debentures		8,000
Trade Receivables	20,000	
Total	9,80,000	9,80,000

You are required to prepare as at 31st March, 2017 :

(*i*) The Balance Sheet of Vanity Ltd. as per Schedule III of the Companies Act, 2013.

(*ii*) Notes to Accounts. [12]

Q. 8. (A) Susan, Geeta and Rashi are partners sharing profits and losses in the ratio of 5 : 3 : 2. Their Balance Sheet as at 31st March, 2017, is as under:

Balance Sheet of Susan, Geeta and Rashi
As at 31st march, 2017

Liabilities	Amount	Assets	Amount
	₹		₹
Sundry Creditors	50,000	Cash at Bank	70,000

Workmen Compensation Reserve		25,000	Sundry Debtors	65,000	
Employees Provident Fund		5,000	*Less :* Provision for		
Bank Loan		55,000	Doubtful Debts	(5,000)	60,000
Capital A/c :			Goodwill		50,000
Susan	2,20,000		Furniture		1,00,000
Geeta	1,70,000		Building		3,80,000
Rashi	1,35,000	5,25,000			
		6,60,000			6,60,000

The partners decided to dissolve their partnership on 31st March, 2017.

The following transactions took palce at the time of dissolution :

- (*a*) Realization expenses of ₹2,000 were paid by Susan on behalf of the firm.
- (*b*) Geeta took over the goodwill for her own business at ₹40,000.
- (*c*) Building was taken over by Rashi at ₹3,00,000.
- (*d*) Only 80% of the debtors paid their dues.
- (*e*) Furniture was sold for ₹97,000.
- (*f*) Bank Loan was settled along with interest of ₹5,000.

You are required to prepare the Realisation Account. [4]

(B) The capital accounts of Amar and Harsh stood at ₹20,000 and ₹30,000 respectively after the necessary adjustments in respect of drawings and net profit for the year ended 31st March, 2017. It was subsequently ascertained that interest on capital @ 12% per annum was not taken into account while arriving at the divisible profits for the year.

During the year 2016-17, Amar had withdrawn ₹2,000 and Harsh's drawings were ₹1,000.

The net profit for the year amounted to ₹15,000.

The partners shared profits and losses in the ratio of 3 : 2.

You are required to pass the necessary journal entries to rectify the error in accounting. [4]

SECTION B (20 Marks)

Answer any two questions

Q. 9. (A) You are required to prepare a Cash-Flow Statement (as per AS-3) for the year 2016-17 from the following Balance Sheets.

Balance Sheets of Honesty Ltd.

As at 31st March, 2016 and 31st March, 2017

Particulars	*Note No.*	*31.3.2017* ₹	*31.3.2016* ₹
I. EQUITY AND LIABILITIES			
1. Shareholder's Funds			

(*a*) Share Capital (Equity Share Capital)		14,00,000	10,00,000
(*b*) Reserves and Surplus (Statement of P/L)		5,00,000	4,00,000
2. Non-Current Liabilities			
Long Term Borrowing (10% Debentures)		5,00,000	1,40,000
3. Current Liabilities			
(*a*) Short Term Borrowings (Bank Overdraft)		20,000	30,000
(*b*) Trade Payables (Creditors)		1,00,000	60,000
(*c*) Short Term Provisions	1	60,000	30,000
TOTAL		25,80,000	16,60,000
II. ASSETS			
1. Non-Current Assets			
Fixed Assets			
(*a*) Tangible	2	16,00,000	9,00,000
(*b*) Intangible (Goodwill)		1,40,000	2,00,000
2. Current Assets			
(*a*) Inventories		2,50,000	2,00,000
(*b*) Trade Receivables		5,00,000	3,00,000
(*c*) Cash and Bank Balances (Cash at Bank)		90,000	60,000
TOTAL		25,80,000	16,60,000

Notes to Accounts :

Particulars	*31.3.2017*	*31.3.2016*
	₹	₹
1. Short term provisions		
Provisions for taxation	60,000	30,000
2. Fixed Assets (Tangible)		
Plant and Machinery	17,60,000	10,00,000
Less : Accumulated Depreciation	(1,60,000)	(1,00,000)
	16,00,000	9,00,000

Additional Information :

During the year 2016-17 :

(*i*) A part of the machine, costing ₹50,000, accumulated depreciation thereon being ₹20,000, was sold for ₹18,000.

(*ii*) Tax paid ₹20,000.

(*iii*) Interest of ₹50,000 paid on Debentures. [8]

(B) State whether the following would result in inflow, outflow or no flow of cash :

(*i*) Bill Receivable endorsed to Creditors.

(*ii*) Old vehicle written off. [2]

Q. 10. (A) Give any two differences between horizontal and vertical analysis of financial statements. [2]

(B) The Quick Ratio of a company is 0.8 : 1. State whether the Quick Ratio will improve, decline or will not change in the following cases :

(*i*) Cash collected from Debtors ₹50,000.

(*ii*) Creditors of ₹20,000 paid off. [2]

(C) From the following information, prepare a Common Size Statement of Profit and Loss of prudence Ltd. for the year ending 31st March, 2017 :

Particulars	*31.03.2017*
	₹
Revenue from Operations	20,00,000
Purchases	15,00,000
Changes in inventories	1,00,000
Other Income (Dividend received)	40,000
Depreciation and Amortization expenses	60,000
Tax Rate @ 40%	

[6]

). 11. (A) Calculate the Net Profit Ratio (up to two decimal places) from the following information :

Particulars	₹
Gross Profit	80,000
Salary and rent	30,000
Interest on Debentures	5,000
Gain on sale of furniture	2,000
Revenue from Operations	4,00,000

[2]

(B) From the following information calculate the following ratios (up to two decimal places) :

(*i*) Earning per share

(*ii*) Price Earning Ratio

(*iii*) Return on Investments

(*iv*) Working Capital Turnover Ratio

Particulars	₹
Net profit after interest and tax	2,40,000
Tax	1,60,000
Net Fixed Assets	10,00,000
Non-current Investments (Non-Trade)	1,00,000
Equity Share Capital (face value ₹10 per share)	5,00,000
15% Preference Share Capital	1,00,000
Reserves and Surplus (including surplus of the year under consideration)	2,00,000
10% Debentures	4,00,000
Revenue from Operations	10,00,000
Working Capital	1,00,000

[8]

Note : The market value of an equity share is ₹40.

SUGGESTED ANSWERS

ISC Annual Examination Question Paper—March, 2018

Q. 2. Refer Latest Examination Q. No. 1 at the end of Chapter 6.

Q. 3. (A) Refer Illustration 10 Chapter 8.

Q. 4. (A) Divisible Profit ₹2,24,400
Hint : Commission 5% on ₹3,64,000 = ₹18,200.

Q. 4. (B) Refer Q. 50 Chapter 4.

Q. 5. Refer Illustration 94 Chapter 3.

Q. 6. (A) Refer Q. 90 Chapter 4.

Q. 6. (B) Refer Illustration 23, Chapter 4.

Q. 7. Refer Illustration 29, Chapter 9.

Q. 8. (A) Loss on Realisation ₹1,08,000.

Q. 8. (B) Refer Illustration 68, Chapter 1.

Q. 9. Refer Illustration 38, Chapter 13.

Q. 10. (A) Refer Chapter 10.

Q. 10. (B) (*i*) No Change; (*ii*) Decline

Q. 10. (C) Refer Illustration 9, Chapter 12.

Q. 11. (A) Net Profit Ratio 11.75%.

Q. 11. (B) Refer Illustration 120, Chapter 14.

I.S.C. ANNUAL EXAMINATION QUESTION PAPER

March, 2019

ACCOUNTS

(Class XII)

(Maximum Marks : 80)

(Time allowed : Three hours)

(Candidates are allowed additional 15 minutes for only reading the paper. They must NOT start writing during this time.)

Part I of Section A is Compulsory

Answer any 4 Questions from Part II of Section A and any two questions from either Section B or Section C.

The intended marks for questions or parts of questions are given in the brackets [].

Transactions should be recorded in the answer book.

All calculations should be shown clearly.

All working, including rough work, should be done on the same page as, and adjacent to, the rest of the answer.

SECTION A

PART I (12 Marks)

Answer all questions.

uestion 1

Answer briefly each of the following questions : [6 × 2]

(*i*) List any two items which may appear on the credit side of a partner's fixed capital account.

(*ii*) Give the journal entries to be passed when :

(*a*) Interest is due on debentures.

(*b*) Interest is paid to debenture holders.

(*iii*) In what way, if any, can the balance in shares forfeited account be used?

(*iv*) Mention any two circumstances when there is need to revalue goodwill of a partnership firm.

(*v*) Enumerate any two methods of redemption of debentures.

(*vi*) Give the journal entry for closing the retiring partner's capital account when his share is paid to him privately by the remaining partners.

PART II (48 Marks)

Answer any four questions.

uestion 2

(A) Meera Co. Ltd. invited applications for 50,000, equity shares of ₹10 each at a premium of ₹2 per share, payable as follows :

On Application on 1st May, 2017	₹2	
On Allotment on 1st July, 2017	₹5	(including premium)
On 1st and Final Call on 1st October, 2017	₹5	

The Company received applications for 62,500 shares.

It was decided to :

(*a*) Refuse allotment to the applicants of 2,500 shares.

(*b*) Allot in full to applicants of 10,000 shares.

(*c*) Allot the balance of the shares applied on a pro-rata basis among the other applicants.

(*d*) Utilize the excess application money in part payment of allotment money.

(*e*) Charge interest on calls-in-arrears, if any, @ 10% per annum.

All the money due was received except from one shareholder to whom 200 shares had been allotted in full. The amount was due by him to the company even till the date of the Balance Sheet, which was 31st March, 2018.

The company charged interest on calls-in-arrears from the shareholder from the date on which it was due till the Balance Sheet date.

You are required to, for the the year 2017-18 :

(*i*) Prepare the Cash Book to record the above issue of shares.

(*ii*) Pass journal entries in the Journal Proper (including entries for interest on calls-in-arrears). [8]

(B) On 31st March, 2018, Vipul Ltd. had ₹30,00,000, 8% Debentures of ₹100 each outstanding.

On 1st June, 2018, it purchased in the open market, 20,000 of its own debentures @ ₹102 per debenture and cancelled these debentures immediately.

On 31st December, 2018, the remaining debentures were purchased @ ₹98 per debenture for immediate cancellation.

You are required to pass necessary journal entries for the redemption of debentures. *(Ignore interest on debentures and entries for provisions regarding Debenture Redemption Reserve and Debenture Redemption Investment).* [4]

Question 3

Mohit, Ali and John are partners in a firm, sharing profits and losses in the ratio of 3 : 1 : 1. Their Balance Sheet as at 31st March, 2018, was as follows :

BALANCE SHEET OF MOHIT, ALI AND JOHN

as at 31st March, 2018

Liabilities		₹	Assets		₹
Trade Creditors		15,000	Cash at Bank		40,000
General Reserve		6,000	Sundry Debtors	30,000	
Investment Fluctuation Fund		9,000	*Less* : Provision for Doubtful Debts	(5,000)	25,000
Capital A/c :			Investments (Market Value ₹40,000)		35,000
Mohit	70,000		Plant & Machinery		88,000
Ali	50,000		Goodwill		12,000
John	50,000	1,70,000			
		2,00,000			2,00,000

Mohit retired on 1st April, 2018, subject to the following adjustments :

(*a*) Goodwill of the firm to be valued at ₹20,000.

(*b*) Mohit to take over the investments at the market value.

(*c*) 25% of the General Reserve to be transferred to Provision for Doubtful Debts and the balance to be distributed amongst all the partners.

(*d*) Creditors to be paid ₹3,000 less.

(*e*) Investment Fluctuation Fund not to be distributed. For this, it was decided that the remaining partners would compensate the retiring partner through their capital accounts.

(*f*) Mohit to be paid ₹20,000 immediately on retirement and the balance to be transferred to his loan account.

You are required to :

(*i*) Pass journal entries on the date of Mohit's retirement.

(*ii*) Prepare the Balance Sheet of the reconstituted firm. [12]

uestion 4

(A) Raina and Meena were partners in a firm sharing profits and losses equally. They dissolved their firm on 31st March, 2018.

On this date, the Balance Sheet of the firm, apart from realizable assets and outside liabilities showed the following :

	₹	
Raina's Capital	40,000	(Cr.)
Meena's Capital	20,000	(Dr.)
Profit and Loss Account	10,000	(Dr.)
Raina's Loan to the firm	15,000	
Contingency Reserve	7,000	

On the date of dissolution of the firm :

(*a*) Raina's loan was repaid by the firm along with interest of ₹500.

(*b*) The dissolution expenses of ₹1,000 were paid by the firm on behalf of Raina who had to bear these expenses.

(*c*) An unrecorded asset of ₹2,000 was taken over by Meena while Raina discharged an unrecorded liability of ₹3,000.

(*d*) The dissolution resulted in a loss of ₹60,000 from the realization of assets and settlement of liabilities.

You are required to prepare :

(*i*) Partner's Capital Account.

(*ii*) Raina's Loan Account. [8]

(B) Vinay, Usha and Punit are partners in a firm. They have been sharing profits and losses in the ratio of 3 : 4 : 1.

Punit wants the profits to be shared equally amongst the partners. He further wants the change in profit sharing ratio to be applicable retrospectively for the last two years. Vinay and Usha have no objection to this.

The profits for the last two years were ₹70,000 and ₹50,000.

You are required to record the adjustment by means of a single journal entry. *(Show the workings clearly).* [4]

Question 5

(A) Peter, Max and Som were partners in a firm sharing profits and losses in the ratio of 4 : 2 : 1. Their fixed capitals were ₹40,000, ₹30,000 and ₹30,000, respectively.

Som was guaranteed a profit of ₹39,000 by the firm.

It was decided that any loss arising because of the guarantee would be shared by Peter and Max equally.

The net profit of the firm for the year ended 31st March, 2018, was ₹1,47,000.

You are required to prepare the Profit and Loss Appropriation Account for the year 2017-18, showing the distribution of profits. [4]

(B) Aditi and Parul are partners in a firm with capitals of ₹35,000 each. They shared profits and losses in the ratio of 3 : 1.

On 1st April, 2017, they admit Chanda into their partnership with 1/5th share in the profits.

Chanda brings in ₹40,000 as her capital and her share of goodwill in cash.

Her share of goodwill is calculated on the basis of her capital contribution and her share of profits in the firm.

At the time of Chanda's admission :

(*a*) The firm had a Workmen Compensation Reserve of ₹60,000 against which there was a claim of ₹20,000.

(*b*) Creditors of ₹8,000 were paid by Aditi privately for which she is not to be reimbursed.

(*c*) There was no change in the value of other assets and liabilities.

You are required to, on the date of Chanda's admission :

(*i*) Calculate the goodwill of the firm. *(Show the workings clearly).*

(*ii*) Pass the necessary journal entries to record the above transactions. [8]

Question 6

Ravi and Tiku are partners in a firm. According to their partnership deed:

(*i*) Interest on capital will be allowed @ 5% per annum.

(*ii*) Interest on drawings will be charged @ 4% per annum.

(*iii*) Each partner will be given a salary of ₹1,000 per month.

(*iv*) Partners will share profits and losses in the ratio of 2 : 1.

Following are the particulars of the capitals and drawings of the partners :

	Ravi	*Tiku*
	₹	₹
Capital (1st April, 2017)	60,000	50,000
Drawings (made on 1st June, 2017)	3,000	6,000

Ravi had taken a loan of ₹10,000 from the firm on which interest of ₹200 was due by him to the firm.

The accounts for the year 2017-18 showed that the firm had made a profit of ₹77,000 before taking into account any interest, partner's salaries and manager's salary of ₹18,000.

You are required to prepare :

(*i*) Profit and Loss Appropriation Account for the year 2017-18,

(*ii*) Partner's Capital Accounts. [12]

estion 7

The trainee accountant of Rudra Ltd. drafted the following Balance Sheet. He did not prepare it according to the format prescribed as per Schedule III of the Companies Act, 2013. He also classified a few items incorrectly.

BALANCE SHEET OF RUDRA LTD.

for the year ending 31st March, 2018

Assets	*Amount*	*Liabilities*	*Amount*
	₹		₹
eneral Reserve	1,20,000	Capital (1,30,000 Equity Shares @ ₹10 each)	13,00,000
ant & Machinery	6,00,000	Share Forfeiture	10,000
nd & Building	8,00,000	Goodwill	1,00,000
ofit & Loss (Debit Balance)	1,50,000	Trade Receivables	20,000
sh & Bank Balances	2,50,000	Trade Payables	50,000
claimed Dividend	30,000	Inventories	30,000
lls-in-arrears (₹4 per share)	40,000		

		Fixed Deposit accepted	4,50,000
		Calls-in-advance	30,000
	19,90,000		19,90,000

Foot note : The company had an authorized capital of 2,00,000 Equity shares of ₹10 each.

You are required to prepare, as at 31st March, 2018 :

(*i*) The Balance Sheet of Rudra Ltd. as per Schedule III of the Companies Act, 2013.

(*ii*) Notes to Accounts.

[12]

Question 8

You are required to pass journal entries to record the following issues of debentures and to write off any capital losses.

(*a*) Zoom Ltd. issues 6,000, 12% Debentures of ₹100 each at par redeemable after 5 years also at par.

(*b*) Zola Ltd. issues 5,000, 13% Debentures of ₹100 each at a discount of 10% to be redeemed at par after 7 years.

(*c*) Zubic Ltd. issues 11% Debentures of the total face value of ₹12,00,000 at a premium of 5% to be redeemed at par after 6 years.

(*d*) Ruby Ltd. issues ₹5,00,000, 12% Debentures at a premium of 5% to be redeemed at 10% premium after 10 years.

(*e*) Emerald Ltd. issues 3,000, 9% Debentures of ₹100 each at a discount of 7%, to be redeemed at a premium of 10% after 4 years.

Note : *All the companies write off their capital losses in the year in which they occur.*

[12]

SECTION B (20 Marks)

Answer any two questions

Question 9

(A) Mention any two commonly used tools for comparison of financial statements. [2]

(B) While preparing Cash Flow Statement, identify the following transactions as belonging to *Operating Activities, Investing Activities, Financing Activities, Cash and Cash Equivalents :*

(*i*) Bank overdraft repaid.

(*ii*) Purchase of Marketable Securities to be sold within 90 days. [2]

(C) From the following data, prepare a Common Size Balance Sheet of Palms Ltd. as at 31st March, 2018 :
(All calculations up to two decimal places)

Particulars	31.03.2018 ₹
Share Capital	24,00,000
Trade Payables	2,40,000
Fixed Assets (Tangible)	20,00,000
Fixed Assets (Intangible)	2,00,000
Reserves and Surplus	3,60,000
Cash and Bank Balances	8,00,000
Short-term Loans and Advances	2,00,000
Short-term Borrowings	40,000
Long-term Borrowings	1,60,000

[6]

Question 10

(A) Calculate the Gross Profit Ratio from the following information :

Particulars	
Opening Inventory	₹ 80,000
Closing Inventory	₹ 1,00,000
Revenue from Operations	₹ 9,00,000
Inventory Turnover Ratio	8 times

[2

(B) From the following Statement of Profit & Loss of Gama Ltd. for the yea 2017-18, calculate (up-to two decimal places) :

(*i*) Net Profit Ratio

(*ii*) Operating Profit Ratio

(*iii*) Current Ratio

(*iv*) Quick Ratio

STATEMENT OF PROFIT AND LOSS OF GAMA LTD.
for the year ending 31st March, 2018

Particulars	*Note No.*	₹
Revenue from Operations		3,00,00
Other Income (Dividend Received)		40,00
Total Revenue		3,40,00
Expenses :		
Purchases		1,80,00
Change in Inventories	1	(4,00
Employee Benefit Expenses (Salaries)		10,0
Depreciation and Amortization (Depreciation of Fixed Assets)		28,0
Other Expenses	2	6,0
Total Expenses		2,20,0
Profit before Tax		1,20,0
Less : Provision for Tax		(48,0
Profit after Tax		72,0

tes to Accounts :

Particulars	₹
1. Change in Inventories :	
Opening Inventory	8,000
Closing Inventory	12,000
	(4,000)
2. Other Expenses :	
Carriage Outward	4,000
Rent	2,000
	6,000

dditional Information :

Total Current Liabilities as on 31st March, 2018	₹50,000
Current Assets (other than inventory) as on 31st March, 2018	₹70,000

[8]

uestion 11

(A) Mention whether the following would result in *inflow*, *outflow* or *no flow* of cash :

(*i*) Issue of fully paid Bonus Shares

(*ii*) Cash withdrawn from Bank [2]

(B) From the following information and extracts of Balance Sheets of Pioneer Ltd. as at 31st March, 2017 and 31st March, 2018, calculate for the year 2017-18 :

(*i*) Cash Flow from Operating Activities

(*ii*) Cash Flow from Investing Activities

Particulars	*31.3.2018*	*31.3.2017*
	₹	₹
General Reserve	40,000	30,000
Balance in Statement of Profit and Loss	2,40,000	1,40,000
Provision for Tax	1,20,000	90,000
Trade Payables	32,000	44,000
Plant and Machinery (at cost)	2,90,000	2,45,000
Accumulated depreciation on Plant and Machinery	30,000	40,000
Patents	50,000	1,50,000
10% Debentures	1,20,000	10,000
Goodwill	15,000	12,000

Note : Proposed dividends for the years 2016-17 and 2017-18 were ₹40,000 and ₹50,000 respectively.

Additional Information :

During the year 2017-18 :

(*a*) The company provided depreciation on Plant and Machinery amounting to ₹24,000.

(*b*) A fully depreciated machine had been condemned and scrapped.

(*c*) Some patents were written off while some patents were sold for ₹75,000 at a profit of ₹5,000. No new patents were purchased.

(*d*) Interest of ₹12,000 paid on Debentures.

(*e*) Tax paid ₹50,000.

(*f*) Dividend proposed in 2016-17 was approved by the shareholders and paid by the company.

SUGGESTED ANSWERS

ISC Annual Examination Question Paper—March, 2019

Q. 1.

(*i*)	(1)	Opening Capital Balance / Initial capital introduced	
	(2)	Additional capital introduced	
(*ii*)	(a)	Interest on Debentures A/c To Debenture holders A/c	Dr.
	(b)	Debenture holders A/c To Bank A/c	Dr.
(*iii*)	(1)	The credit balance in the forfeiture shares account is used to make up the deficiency if forfeited shares are reissued at a discount.	
	(2)	Any amount remaining in forfeited shares account after writing off the discount on reissue is a capital profit which should be transferred to Capital Reserve and used to write off capital losses.	
(*iv*)		Any two points : • Admission of a partner • Retirement of a partner • Death of a partner • Change in profit sharign ratio amongst the partners • Sale of a firm • Amalgamation of two or more firms • Partnership firm converted into a company	
(*v*)		Any two methods : • By payment in lump sum to the debenture holders at the end of a specific period. • By payment in instalments to the debenture holders by draw of lots. • By purchase of own debentures in the open market. • By conversion of debentures into shares or new debentures.	
(*vi*)		Retiring / Outgoing Partner's Capital A/c To Remaining / Continuing Partner's Capital A/cs	Dr.

Q. 2. **(A)** Refer Latest Examination Q. No. 2 at the end of Chapter 6.

(B) Refer Illustration 18 Chapter 8

Q. 3. Refer Q. 91 Chapter 4.

Q. 4. **(A)** Refer Q. 54 Chapter 5.

(B) Refer Q. 91 Chapter 1

Q. 5. **(A)** Refer Q. 100 Chapter 1

(B) Refer Illustration 67 Chapter 3

Q. 6. Refer Q. 80 Chapter 1

Q. 7. Refer Illustration 30 Chapter 9

Q. 8. Refer Illustration 18 Chapter 7

Q. 9. **(A)** (*i*) Comparative financial statements

(*ii*) Common size financial statements

(B) (*i*) Bank overdraft repaid is financing activity.

(*ii*) Purchase of marketable securities is Cash and Cash Equivalent.

(C) Refer Illustration 3 Chapter 12

Q. 10. **(A)** G.P. Ratio 20%.

(B) Refer Illustration 121 Chapter 14

Q. 11. **(A)** (*i*) Issue of fully paid bonus shares : No Flow

(*ii*) Cash withdrawn from bank : No Flow

(B) Refer Q. 67 Chaper 13

I.S.C. ANNUAL EXAMINATION QUESTION PAPER

March, 2020

ACCOUNTS

(Class XII)

(Maximum Marks : 80)

(Time allowed : Three hours)

*(Candidates are allowed additional 15 minutes for **only** reading the paper. They must NOT start writing during this time.)*

***Part I of Section A** is Compulsory.*

*Answer **any 4** Questions from **Part II of Section A** and **any two** questions from **either Section B or Section C.***

The intended marks for questions or parts of questions are given in the brackets [].

Transactions should be recorded in the answer book.

All calculations should be shown clearly.

All working, including rough work, should be done on the same page as, and adjacent to, the rest of the answer.

SECTION A

PART I (12 Marks)

Answer all questions.

Q. 1. Answer briefly each of the following questions : [6 × 2]

(*i*) Why is goodwill considered to be an intangible asset and not a fictitious asset?

(*ii*) How will a firm deal with a situation when its partnership deed provides for interest on capital, but the profit earned by it is not enough to do so, at the rate mentioned in the deed?

(*iii*) State with reason whether Securities Premium Reserve can be used by a company to write off the discount allowed to its debtors.

(*iv*) List *any four* items that are shown under the sub-head 'Other Current Assets' in the Balance Sheet of a company prepared as per Schedule III of the Companies Act, 2013.

(*v*) What is the maximum limit of debentures which companies, other than Banking Companies and All India Financial Institutions, can redeem out of capital?

(*vi*) (*a*) Mention *any two* circumstances which can lead to dissolution of partnership.

(*b*) What is the status of the firm upon the dissolution of partnership?

PART II (48 Marks)

Answer any four questions.

Q. 2. (A) From the following information, calculate goodwill of the firm of Anmol and Sujay at the time of admission of Dhruv :

(*i*) At three years' purchase of Super Profit.

(*ii*) On the basis of Capitalisation of Super Profit.

(*a*) Actual Average Profits of the firm for the last three years is ₹25,000.

(*b*) Normal Rate of Return is 10%.

(*c*) BALANCE SHEET OF ANMOL AND SUJAY

as at 31st March, 2019

Liabilities		₹	*Assets*	₹
Sundry Creditors		40,000	Plant and Machinery	40,000
Bills Payable		10,000	Land and Building	80,000
General Reserve		20,000	Investments (Non-trade)	50,000
Capital Accounts :			Sundry Debtors	15,000
Anmol	80,000		Bank	55,000
Sujay	90,000	1,70,000		
		2,40,000		2,40,000

[4]

Q. 2. (B) Manoj, Hari and Karan are partners in a firm sharing profits and losses in the ratio 4 : 2 : 1. Their Balance Sheet as at 31st March, 2019, was as follows :

BALANCE SHEET OF MANOJ, HARI AND KARAN

as at 31st March, 2019

Liabilities		₹	*Assets*	₹
Sundry Creditors		32,600	Plant and Machinery	20,000
Bills Payable		4,000	Goodwill	7,000
General Reserve		8,400	Stock	38,000
Capital Accounts :			Bank	20,000
Manoj	16,000			
Hari	14,000			
Karan	10,000	40,000		
		85,000		85,000

Hari retired from the business on 1st April, 2019. The remaining partners decide o carry on the business. The terms of retirement provided the following :

(*a*) Out of the total insurance premium paid, ₹7,000 to be treated as prepai insurance. The amount was earlier debited to Profit & Loss Account.

(*b*) General Reserve not to be distributed.

(*c*) Hari to be paid ₹24,400 in full settlement.

You are required to prepare Partner's Capital Accounts. [8]

Q. 3. Sudesh Ltd. was registered with an authorised capital of ₹40,00,000 divided into 4,00,000 Equity Shares of ₹10 each.

The company offered 50,000 shares to the public at a premium of ₹2 per share, payable as follows :

₹3 on application
₹6 on allotment (including premium)
₹3 on first and final call (due two months after allotment)

Applications were received for 60,000 shares and pro-rata allotment was made as follows :

Category A : The applicants of 40,000 shares were allotted 30,000 shares.

Category B : The applicants of 20,000 shares were allotted in full.

Excess money paid on application was utilized towards allotment.

Nobby, a shareholder from Category A, who had applied for 1,200 shares failed to pay the allotment and call money.

Vineet, a shareholder from Category B, who had been allotted 1,000 shares, paid the call money due, along with allotment.

The company forfeited Nobby's shares after the first and final call and paid interest on Calls-in-advance to Vineet @ 12% per annum on the day of the final call.

You are required to :

(*i*) Pass journal entries to record the above transactions in the books of the company (including entries for interest on Calls-in-advance).

(*ii*) Prepare Calls-in-arrears Account. [12]

Q. 4. (A) Mike and Ajay are partners sharing profits and losses in proportion to their capitals, which on 31st March, 2019, stood at ₹6,00,000 and ₹4,00,000 respectively. On this date, the firm had ₹1,00,000 in its Workmen Compensation Reserve and its outside liabilities amounted to ₹6,00,000, which included Creditors of ₹2,00,000 and Bills Payable of ₹60,000.

The firm was dissolved on 31st March, 2019, on which date, the assets, apart from Cash of ₹70,000, realised ₹14,00,000 and the liabilities were discharged as follows :

(*a*) Creditors due on 31st May, 2019, were paid off at a discount of 3% per annum.

(*b*) Bills Payable were discharged at a rebate of ₹1,000.

(*c*) Workmen Compensation Claim of ₹40,000 was met.

(*d*) Expenses of dissolution amounting to ₹30,000 were paid.

You are required to prepare :

(*i*) Realisation Account.

(*ii*) Partners' Capital Accounts. [8]

Q. 4. (B) Xen, Sam and Tim are partners in a firm. For the year ended 31st March, 2019, the profits of the firm ₹1,20,000, were distributed *equally* amongst them, without providing for the following provisions of the partnership deed :

(*a*) Sam's guarantee to the firm that the firm would earn a profit of at least ₹1,35,000. Any shortfall in these profits would be personally met by him.

(*b*) Profits to be shared in the ratio of 2 : 2 : 1.

You are required to pass the necessary journal entries to rectify the error in accounting. [4]

Q. 5. (A) Zee Ltd. purchased a running business from Rainbow Ltd. for a sum of ₹6,60,000. Zee Ltd. paid 5% of the purchase consideration by drawing a Promissory Note in favour of Rainbow Ltd. and the balance by the issue of fully paid 7% Debentures of ₹100 each at a premium of 10%. The assets and liabilities of Rainbow Ltd. consisted of :

	₹
Fixed Assets	6,50,000
Sundry Creditors	80,000

You are required to pass the necessary journal entries in the books of Zee Ltd. [4]

Q. 5. (B) On 1st April, 2016, the following balances appeared in the books of Shikhar Ltd. *(an unlisted company)*

	₹
10% Debentures	14,00,000
Premium on Redemption of Debentures	1,40,000
Debenture Redemption Reserve	75,000

The debentures were to be redeemed at a premium of 10% in *two equal annual instalments* beginning from 31st March, 2018. To meet the requirements of the Companies Act, 2013, the company transferred the balance amount to Debenture Redemption Reserve on 31st March, 2017. On 30th April, 2017, it met the requirements of the Companies Act, 2013 regarding Debenture Redemption Investment and redeemed the debentures on the scheduled dates.

You are required to pass necessary journal entries to record the above transactions in the books of Shikhar Ltd. *(Ignore interest on Debentures).* [8]

Q. 6. Anita and Tony, each doing business as sole proprietors, started a partnership on 1st April, 2018. Anita brought in Plant and Machinery valued at ₹5,00,000 whereas Tony brought in furniture costing ₹50,000 and ₹7,00,000 in cash.

Since the business needed more funds, Tony gave a loan of ₹2,00,000 to the firm on 30th June, 2018.

Their partnership deed provided for :

(*a*) Interest on capital to be allowed @ 10% per annum.

(*b*) Interest on drawings to be charged @ 6% per annum.

(*c*) Anita to be given a commission of 4% on the *corrected* net profits before charging commission.

(*d*) Tony to be given a salary of ₹12,000 per annum.

Tony withdrew ₹5,000 at the end of every month and Anita withdrew ₹30,000 on 1st August, 2018.

The net profit of the firm, for the year 2018-19, *after* debiting Tony's salary of ₹12,000 per annum but *before* considering any interest due to and due from the partners, was ₹4,00,000.

You are required to prepare for the year 2018-19 :

(*i*) Profit and Loss Appropriation Account.

(*ii*) Partners' Capital Accounts. [12]

Q. 7. Smita and Punita are partners in a firm sharing profits and losses in the ratio of 3 : 2. Their Balance Sheet as at 31st March, 2019, is as follows :

BALANCE SHEET OF SMITA AND PUNITA

as at 31st March, 2019

Liabilities		₹	*Assets*		₹
Sundry Creditors		14,000	Cash in hand		30,000
Bank Loan		6,000	Sundry Debtors.	22,000	
General Reserve		10,000	*Less* : Provision for		
Capital Accounts :			doubtful debts	(2000)	20,000
Smita	30,000		Furniture		10,000
Punita	40,000	70,000	Stock		40,000
		1,00,000			1,00,000

On 1st April, 2019, Mita is admitted as a new partner on the following terms :

(*a*) The new profit sharing ratio of Smita, Punita and Mita to be 5 : 3 : 2.

(*b*) Provision for doubtful debts to be raised to 10% of the debtors.

(*c*) Punita to take over the firm's investments (not recorded in the books) at ₹3,000.

(*d*) Goodwill of the firm to be valued at ₹50,000. Mita to bring in cash for her share of goodwill.

(*e*) 50% of the goodwill to be withdrawn by the old partners.

(*f*) Mita to pay off the Bank Loan on behalf of the firm. The amount due to her by the firm, to be considered as part of her capital contribution.

(*g*) Mita to bring in the balance of her capital in cash, so as to make her capital equal to 1/5th of the total capital of the firm.

You are required to :

(*i*) Pass journal entries at the time of Mita's admission.

(*ii*) Prepare the Balance Sheet of the reconstituted firm. [12]

Q. 8. (A) Xylo Ltd. was formed on 1st April, 2017, with an authorized capital of ₹12,00,000 divided into Equity Shares of ₹10 each. It issued a prospectus inviting applications for 30,000 shares to be issued at par. The issue was fully subscribed and the amount due on the shares was received by the company.

On 1st April, 2018, the company issued another 60,000 shares at a premium of ₹2 per share to be received with allotment. Applications for 55,000 shares were received which were duly allotted.

All the amounts due on these shares were received except the final call of ₹2 per share on 1,000 shares.

On 1st October, 2018, the company also issued 2,000 *6% debentures of ₹100 each* at par, to be redeemed at par in *five equal annual instalments* beginning from 1st October, 2019. The entire issue price of these debentures was received by the company with application.

Half yearly interest on the debentures of ₹6,000 was paid by the company to the debenture holders on 31st March, 2019.

You are required to show the relevant items under :

(*i*) Equity and Liabilities in the Balance Sheet of the Company as at 31st March, 2019 (prepared as per Schedule III of the Companies Act, 2013).

(*ii*) Notes to Accounts. [8]

Q. 8. (B) Under which heads and sub-heads will the following items appear in the Balance Sheet of a company as per Schedule III of the Companies Act, 2013 :

(*i*) Trade Debtors

(*ii*) Marketable Securities

(*iii*) Finished Goods

(*iv*) Patents [4]

SECTION B (20 Marks)

Answer any two questions

Q. 9 (A) Assuming that the current ratio of a company is 0.7 : 1, mention whether this ratio would *increase, decrease* or *not change* after the following transactions :

(*i*) Payment of ₹15,000 made to a creditor.

(*ii*) Purchase of inventory worth ₹1,00,000 on credit. [2]

Q. 9. (B) Prepare a Comparative Statement of Profit and Loss of Cosmos Ltd. from the following information :

Particulars	*31.03.2019*	*31.03.2018*
Revenue from Operations	₹20,00,000	₹10,00,000
Purchases of stock-in-trade	₹12,00,000	₹6,00,000
Change in Inventories of Stock-in-trade	25% of purchases of stock-in-trade	20% of purchases of stock-in-trade
Other Expenses	₹1,00,000	₹80,000
Tax Rate	40%	40%

[6]

Q. 9. (C) From the following extract of the Balance Sheet of Regal Ltd., taking into consideration the additional information, you are required to calculate the amounts of the following items to be shown in the company's Cash Flow Statement for the year 2018-19 :

(*i*) Fixed asset purchased.

(*ii*) Fixed asset sold.

(*iii*) Profit/Loss on sale of fixed asset.

(*iv*) Depreciation charged on fixed assets.

Particulars	*31.03.2019* (₹)	*31.03.2018* (₹)
Fixed Asset	6,00,000	4,90,000

Additional information

(*i*) The provision for depreciation on fixed assets stood at ₹1,40,000 on 31st March, 2018 and ₹1,80,000 on 31st March, 2019.

(*ii*) During the year 2018-19, a fixed asset costing ₹60,000 (book value ₹30,000) was sold for ₹20,000. [2]

Q. 10. You are required to prepare a Cash-Flow Statement (as per AS-3) for the year 2018-19 from the following Balance Sheets :

BALANCE SHEET OF HILLOCK LTD.
as at 31st March, 2018 and 31st March 2019

Particulars	*Note No.*	*31.3.2019*	*31.3.2018*
		₹	₹
I. EQUITY AND LIABILITIES :			
1. **Shareholder's Funds :**			
(*a*) Equity Share Capital		2,50,000	2,00,000
(*b*) Reserve and Surplus	1	90,000	50,000
2. **Current Liabilities :**			
(*a*) Short-term Borrowings (Bank overdraft)		—	10,000
(*b*) Trade Payables		20,000	15,000
(*c*) Other Current Liabilities	2	5,000	5,000
(*d*) Short-term Provisions (Provision for Tax)		25,000	20,000
Total		3,90,000	3,00,000
II. ASSETS :			
1. **Non-Current Assets :**			
Fixed Assets – Tangible		2,55,000	2,35,000
2. **Current Assets :**			
(*a*) Current Investments		30,000	—
(*b*) Inventories		15,000	25,000
(*c*) Trade Receivables		40,000	10,000
(*d*) Cash and Bank Balances		50,000	30,000
Total		3,90,000	3,00,000

Notes to Accounts :

	31.3.2019	31.3.2018
(1) Reserves and Surplus		
Balance in Statement of Profit and Loss	70,000	40,000
Securities Premium Reserve	20,000	10,000
	90,000	50,000
(2) Other Current Liabilities		
Outstanding Expenses	1,000	5,000
Unclaimed Dividend	4,000	—
	5,000	5,000
(3) Contingent Liability :		
Proposed Dividend	5,000	10,000

Additional Information :

During the year 2018-19 :

(*i*) A tangible fixed asset costing ₹50,000 was purchased.

(*ii*) Tax paid ₹15,000.

(*iii*) Interest of ₹1,000 was paid on the bank overdraft. [10]

Q. 11. (A) State the objective of calculating Liquidity Ratios. [2]

Q. 11. (B) From the following information, calculate Earnings per share *(up to two decimal places)* :

Particulars	₹
10% Preference Share Capital	6,00,000
Equity Share Capital (3,00,000 shares of ₹10 each)	30,00,000
Profit before Tax	15,00,000
Tax Rate	30%

[2]

Q. 11. (C) From the following information, calculate the following ratios (up to two decimal places) :

(*i*) Debt to Total Assets Ratio

(*ii*) Proprietary Ratio

(*iii*) Inventory Turnover Ratio

Particulars	₹
Fixed Assets	14,00,000
Current Assets (including inventory of ₹2,00,000)	10,00,000
Shareholders' Funds	14,40,000
Non-Current Liabilities (10% Long-term Bank Loan)	8,00,000
Current Liabilities	5,00,000
Revenue from Operations	15,00,000
Gross Profit	6,00,000

[6]

SUGGESTED ANSWERS

ISC Annual Examination Question Paper—March, 2020

Q. 1. (*i*) Goodwill cannot be seen or touched, it can only be felt. Hence, it is treated as an intangible asset. But it is not a fictitious asset because fictitious assets do not have a value whereas goodwill has a value and it can be purchased or sold with any other asset.

(*ii*) The available profit will be distributed among the partners in the ratio of interest on capital.

(*iii*) 'Securities Premium Reserve' cannot be used to write off the discount allowed to its debtors. It is a capital profit and can be used only for those purposes which are specified under section 52 of Companies Act, 2013. Discount allowed to debtors is a revenue expense and charge against profits.

(*iv*) Other Current Assets include :
Prepaid Expenses, Interest accrued on Investments, Advance Tax, Dividend receivable, any capital loss to be written off in the next financial/accounting year.

(*v*) Listed companies are not required to create any Debenture Redemption Reserve. Hence, they can redeem all the debentures out of capital.

(*vi*) Unlisted companies are required to create Debenture Redemption Reserve equal to atleast 10% of outstanding debentures out of divisible profits. Hence, they can redeem 90% of their debentures out of capital.

(*vii*) (*a*) Dissolution of Partnership arises in case of
- Change in the constitution of partnership;
- Admission/Retirement/Death of a partner;
- Change in profit sharing ratio; etc.

(*b*) Dissolution of partnership may or may not result into closing down of the business as the remaining partners may agree to carry on the business under a new agreement.

Q. 2. **(A)** Refer Illustration 18 Chapter 2

(B) Refer Illustration 71 Chapter 4

Q. 3. Refer Latest Examination Question No. 3 at the end of Chapter 6

Q. 4. **(A)** Refer Q. 59 Chapter 5.

(B) Refer Illustration 70 Chapter 1

Q. 5. **(A)** Refer Illustration 6 Chapter 7

(B) Refer Illustration 16 Chapter 8

Q. 6. Refer Illustration 27 Chapter 1

Q. 7. Refer Q. 130 Chapter 3

Q. 8. **(A)** Refer Q. 31 Chapter 9

(B) Refer Q. 30 Chapter 9

Q. 9. **(A)** (*i*) Decrease (*ii*) Increase

(B) Refer Q. 38 Chapter 11

(C) Refer Q. 68 Chapter 13

Q. 10. Refer Q. 69 Chapter 13

Q. 11. **(B)** Earning Per Share ₹3.30

(C) Refer Illustration 122 Chapter 14

ANSWERS OF MULTIPLE CHOICE QUESTIONS

Chapter 6

Company Accounts—Issue of Shares

(A) Answers of of Case Based MCQs :

1. (a) **Ans.** (*ii*) ₹30,00,000

   (b) **Ans.** (*iv*) ₹27,30,000

   (c) **Ans.** (*iii*) ₹27,00,000

   (d) **Ans.** (*ii*) ₹ 30,000

Hint :

Issued Capital :			₹
30,000 Equity Shares of ₹100 each			30,00,000
Subscribed Capital :			
Subscribed and Fully Paid Capital :			
27,000 Equity Shares of ₹100 each fully called up		27,00,000	
Subscribed but not Fully Paid Capital :			
1,000 Equity Shares of ₹100 each fully Called up	1,00,000		
Less : Calls in Arrears (1,000 Shares × ₹70*)	70,000	30,000	27,30,000

*	Calls in Arrears		₹
	On Allotment	: 1,000 shares @ ₹30 (excluding premium)	30,000
	On First & Final Call	: 1,000 shares @ ₹40	40,000
			70,000

(e) **Ans.** (*ii*) ₹10,80,000

	₹
Securities Premium Reserve 28,000 shares @ ₹40	11,20,000
Less : Calls in Arrears 1,000 shares @ ₹40	40,000
	10,80,000

2. (a) **Ans.** (*ii*) ₹10,000

Hint :

Date	*Particulars*		*L.F.*	*Dr. Amount*	*Cr. Amount*
				₹	₹
	Share Capital A/c	Dr.		20,000	
	Securities Premium Reserve A/c	Dr.		36,000	
	To Calls in Arrears A/c				46,000
	To Share Forfeiture A/c				10,000

   (b) **Ans.** (*i*) ₹36,000

   (c) **Ans.** (*iv*) ₹46,000

   (d) **Ans.** (*i*) Face Value

3. (a) **Ans.** (*iii*) ₹4,800

Hint : Share Capital Account is debited by Called up amount on shares (excluding premium) :

	₹
On Application	3
On Allotment	3
	6

Called up amount on 800 shares = 800 × ₹6 = ₹4,800

Entry on Forfeiture :

Date	Particulars		L.F.	Dr. Amount	Cr. Amount
				₹	₹
	Share Capital A/c (800 × ₹6)	Dr.		4,800	
	Securities Premium Reserve A/c (800 × ₹4)	Dr.		3,200	
	To Calls in Arrears A/c (800 × ₹7)				5,600
	To Share Forfeiture A/c				2,400

(b) **Ans.** (*iii*) ₹3,200

(c) **Ans.** (*iv*) ₹2,400

(d) **Ans.** (*ii*) Profit earned by a company after its incorporation.

4. (a) **Ans.** (*iv*) ₹8,000

Hint :

Date	Particulars		L.F.	Dr. Amount	Cr. Amount
				₹	₹
(*i*)	Share Capital A/c (3,000 × ₹16)	Dr.		48,000	
	Securities Premium Reserve A/c	Dr.		30,000	
	To Calls in Arrears A/c				60,000
	To Share Forfeiture A/c				18,000
(*ii*)	Bank A/c	Dr.		28,000	
	Share Forfeiture A/c	Dr.		4,000	
	To Share Capital A/c				32,000
(*iii*)	Share Forfeiture A/c	Dr.		8,000	
	To Capital Reserve A/c				8,000

(b) **Ans.** (*iii*) ₹6,000

(c) **Ans.** (*ii*) NIL

(d) **Ans.** (*ii*) ₹5,82,000

Hint :

36,000 Shares of ₹20 each, ₹16 called	5,76,000
Add : Share Forfeiture A/c	6,000
	5,82,000

(e) **Ans.** (*ii*) Issuing partly paid bonus shares to shareholders.

5. (a) **Ans.** (*iii*) ₹13,000

Hint :

	₹
Amount not paid on allotment (including premium)	13
Amount not paid on first call (including premium)	13
	26

Calls in Arrears = 500 Shares × ₹26 = ₹13,000

Entry on Forfeiture :

Share Capital A/c	Dr. 7,500	
Securities Premium Reserve A/c	Dr. 7,500	
To Calls in Arrears A/c		13,000
To Share Forfeiture A/c		2,000

(b) **Ans.** (*ii*) ₹7,500

(c) **Ans.** (*iv*) ₹2,000

(d) **Ans.** (*iii*) ₹7,500

6. (a) **Ans.** (*ii*) ₹9,00,000

(b) **Ans.** (*iv*) 84,800

(c) **Ans.** (*iv*) 8,49,600

Hint :

	₹
Subscribed and Fully Paid Capital	
84,800 Shares of ₹10 each fully paid	8,48,000
Add : Share Forfeiture Account	
(₹8 per share received on 200 unissued shares)	1,600
	8,49,600

(d) **Ans.** (*ii*) Capital Reserve Account

7. (a) **Ans.** (*ii*) ₹21,000

(b) **Ans.** (*iv*) Nil

(c) **Ans.** (*ii*) 29,33,000

Hint :

		₹
Subscribed but not Fully Paid Capital		
3,68,000 Shares of ₹10 each, ₹8 called up	29,44,000	
Less : Calls in Arrears (7,000× ₹3)	21,000	
	29,23,000	
Add : Share Forfeiture A/c	10,000	29,33,000

(d) **Ans.** (*ii*) Subscribed Capital

(e) **Ans.** (*iii*) Distribution of Dividend

8. (d) **Ans.** (*iii*) ₹98,000

Hints :

I. Excess amount received from Raghu on application :

Shares Allotted to Raghu = $7,000 \times \frac{2,00,000}{3,50,000} = 4,000$

Excess application money received from Raghu :
7,000 Shares – 4,000 Shares = 3,000 Shares × ₹4 = ₹12,000

		₹
II.	Amount due from Raghu on Allotment :	14,000
	4,000 Shares × ₹3.50	12,000
	Less : Excess received from Raghu on Application	2,000
	Allotment money not received from Raghu	
III	Total amount due on Allotment : 2,00,000 Shares × ₹3.50	7,00,000
	Less : Excess amount received on Application	6,00,000
	Balance Due	1,00,000
	Less : Amount not received from Raghu on Allotment	2,000
	Net amount received on Allotment in Cash	98,000

(b) **Ans.** (*iii*) ₹18,000

Hint : Entry on Forfeiture of Raghu's shares :

Date	*Particulars*		*L.F.*	*Dr. Amount*	*Cr. Amount*
				₹	₹
	Equity Share Capital A/c	Dr.		20,000	
	To Calls in Arrears A/c				2,000
	To Share Forfeited A/c				18,000
	(Raghu's 4,000 shares forfeited)				

(c) **Ans.** (*ii*) ₹27,500

Hint :

Shares allotted to Nandan $10{,}500 \times \frac{2{,}00{,}000}{3{,}50{,}000} = 6{,}000$

Forfeited shares include 1,000 shares of Raghu and 6,000 shares of Nandan

		₹
Forfeited amount on Raghu's 4,000 shares	= 18,000	
As such, Forfeited amount on his 1,000 shares	$\frac{18{,}000}{4{,}000} \times 1{,}000 =$	4,500
Forfeited amount on Nandan's 6,000 shares	=	30,000
		34,500
Less : Loss on Reissue		7,000
Transferred to Capital Reserve		27,500

(d) **Ans.** (*iv*) ₹5,27,500

Hint :

	₹
Reserve and Surplus	
Securities Premium Reserve (2,00,000 × 2.50)	5,00,000
Capital Reserve	27,500
	5,27,500

(e) **Ans.** (*ii*) ₹19,83,500

Hint :

Subscribed and Fully paid Capital	19,70,000
Add : Share Forfeiture Account	13,500
	19,83,500

9. (a) **Ans.** (*iii*) ₹54,000

Hint :

A. Shares allotted to Rohini : $7{,}500 \times \frac{2{,}40{,}000}{3{,}00{,}000} = 6{,}000$

Excess amount received from Rohini on application :

7,500 shares – 6,000 shares = 1,500 shares × ₹4 = 6,000

B. Amount Due from Rohini on Allotment : 6,000 × ₹4 =	24,000
Less : Excess received from her on application :	6,000
Amount not received from Rohini on Allotment	18,000
Amount not received from Rohini on Final Call : 6,000 × ₹6	36,000
Calls in Arrears	54,000

(b) **Ans.** (*i*) ₹7,200

Hint

Date	Particulars	L.F.	Dr. Amount ₹	Cr. Amount ₹
	Share Capital A/c Dr.		60,000	
	Securities Premium Reserve A/c Dr.		12,000	
	To Calls in Arrears A/c			54,000
	To Share Forfeiture A/c			18,000
	(6,000 shares forfeited)			
	Bank A/c Dr.		26,400	
	To Share Capital A/c			24,000
	To Securities Premium Reserve A/c			2,400
	(2,400 shares reissued @ ₹11 each)			
	Share Forfeiture A/c Dr.		7,200	
	To Capital Reserve A/c*			7,200
	(Gain on reissue)			

* $18{,}000 \times \frac{2{,}400}{6{,}000} = ₹7{,}200$

(c) **Ans.** (*iv*) ₹9,50,400

Hint :

Total Securities Premium Reserve : 2,40,000 × ₹4	9,60,000
Less : Debited in Forfeiture entry	12,000
	9,48,000
Add : Credited in Reissue entry	2,400
	9,50,400

(d) **Ans.** (*ii*) ₹9,57,600

Hint :

Reserve and Surplus :	
Balance in Securities Premium Reserve	9,50,400
Capital Reserve	7,200
	9,57,600

(e) **Ans.** (*iii*) ₹23,74,800

Hint :

Subscribed and Fully Paid Capital : 2,36,400 shares of ₹10 each	23,64,000
Add : Balance in Share Forfeiture Account (₹18,000 – ₹7,200)	10,800
	23,74,800

10. (a) **Ans.** (*iv*) ₹7,60,000

Hint :

I. Shares applied by Seema : $4{,}000 \times \frac{1{,}00{,}000}{80{,}000} = 5{,}000$

Excess application money paid by Seema = (5,000 – 4,000) × ₹20 = ₹20,000

		₹
II. Amount due from Seema on Allotment = 4,000 × ₹15	=	60,000
Less : Excess received from her on Application		20,000
Calls in Arrears from Seema		40,000
III. Total Amount due on Allotment : 80,000 × ₹15		12,00,000
Less : Excess received on Application		4,00,000
		8,00,000
Less : Calls in Arrears from Seema		40,000
Net amount received on Allotment		7,60,000

(b) **Ans.** (*ii*) ₹50,000

Hint : Shares allotted to Sahaj : $2{,}500 \times \frac{80{,}000}{1{,}00{,}000} = 2{,}000$

Hint : Entry on forfeiture of Sahaj's shares :

Date	*Particulars*		*L.F.*	*Dr. Amount*	*Cr. Amount*
				₹	₹
	Equity Share Capital A/c (2,000 × ₹40)	Dr.		80,000	
	To Calls in Arrears A/c				30,000
	To Share Forfeiture A/c				50,000
	(Forfeiture of 2,000 shares of Sahaj)				

(c) **Ans.** (*i*) ₹18,400

Hint :

		₹
Forfeited amount on 800 Reissued shares = $50{,}000 \times \frac{800}{2{,}000}$	=	20,000
Less : Loss on Reissue : 800 × ₹2		1,600
Transferred to Capital Reserve		18,400

(d) **Ans.** (*iii*) ₹31,82,000

Subscribed but not fully paid Capital : 78,800 shares of ₹50 each, ₹40 Called-up	31,52,000
Add : Share Forfeiture A/c	30,000
	31,82,000

11. (a) **Ans.** (*iv*) ₹12,73,600

Hints :

I. Shares applied by Agam = $\frac{2,40,000}{2,00,000}$ × 1,000 Shares = 1,200 Shares

		₹
Excess application money received from her = 1,200 – 1,000 = 200 Shares × ₹3	=	600

II. Amount due from Agam on Allotment = 1,000 × ₹7	=	7,000
Less : Excess received on application	=	600
Amount not paid by Agam on allotment		6,400

		₹
III. Total Amount due on Allotment : 2,00,000 Shares × ₹7	=	14,00,000
Less : Excess received on application	=	1,20,000
		12,80,000
Less : Not received from Agam on allotment		6,400
		12,73,600

(b) **Ans.** (*i*) ₹2,600

Hint : Journal Entry on Forfeiture of Agam's shares :

Date	*Particulars*		*L.F.*	*Dr. Amount* ₹	*Cr. Amount* ₹
	Equity Share Capital A/c	Dr.		4,000	
	Securities Premium Reserve A/c	Dr.		5,000	
	To Calls in Arrears A/c				6,400
	To Share Forfeiture A/c				2,600

(c) **Ans.** (*ii*) ₹5,300

Hint :

Forfeited Amount on Agam's 500 shares	= 2,600 × $\frac{500}{1,000}$	=	1,300
Forfeited Amount on Seema's 1,000 shares	= 8,000 × $\frac{1,000}{2,000}$	=	4,000
Capital Reserve			5,300

(d) **Ans.** (*iii*) ₹12,14,300

Hint :

Reserve and Surplus :	
Securities Premium Reserve	12,09,000
Capital Reserve	5,300
	12,14,300

(e) **Ans.** (*iii*) Share Capital

(B) Answers of Multiple Choice Questions :

1. D	2. B	3. C	4. B	5. C
6. A	7. C	8. B	9. B	10. D
11. D	12. C	13. A	14. B	15. D

16.	A	17.	C	18.	B	19.	C	20.	A
21.	D	22.	C	23.	D	24.	B	25.	C
26.	D	27.	B	28.	D	29.	D	30.	D
31.	C	32.	B	33.	C	34.	D	35.	C
36.	A	37.	C	38.	A	39.	B	40.	C
41.	D	42.	D	43.	A	44.	C	45.	C
46.	B	47.	C	48.	B	49.	B	50.	C
51.	B	52.	A	53.	C	54.	B	55.	D
56.	B	57.	C	58.	A	59.	A	60.	D
61.	C	62.	D	63.	D	64.	B	65.	B
66.	B	67.	C	68.	B	69.	B	70.	A
71.	D	72.	D	73.	B	74.	D	75.	D
76.	D	77.	B	78.	A	79.	A	80.	D
81.	C	82.	B	83.	A	84.	C	85.	C
86.	C	87.	B	88.	B	89.	B	90.	A
91.	A	92.	C	93.	B	94.	C	95.	C
96.	A	97.	B	98.	C	99.	C	100.	B
101.	C	102.	B	103.	B	104.	C	105.	B
106.	A	107.	C	108.	C	109.	D	110.	C
111.	B	112.	C	113.	D	114.	B	115.	A
116.	D	117.	A	118.	C	119.	D	120.	A
121.	D	122.	C	123.	D	124.	B	125.	B
126.	A	127.	C	128.	C	129.	A	130.	D
131.	A	132.	D	133.	B	134.	D	135.	C
136.	B	137.	C	138.	C	139.	C	140.	C
141.	C	142.	C	143.	A				

Chapter [illegible]

Company Accounts — Issue of Debentures

Answers of Multiple Choice Questions :

1.	C	2.	A	3.	C	4.	B	5.	D
6.	C	7.	D	8.	B	9.	B	10.	B
11.	A	12.	C	13.	B	14.	B	15.	D
16.	D	17.	A	18.	B	19.	D	20.	A
21.	B	22.	C	23.	B	24.	B	25.	A
26.	A	27.	B	28.	D	29.	D	30.	C
31.	B	32.	C	33.	D	34.	B	35.	C
36.	A	37.	C						

Chapter 8

Redemption of Debentures

Answers of Multiple Choice Questions :

1.	C	2.	D	3.	D	4.	D	5.	B
6.	D	7.	B	8.	B	9.	C	10.	A

Chapter 9

Financial Statements of Companies

Answers of Multiple Choice Questions :

1.	D	2.	B	3.	B	4.	D	5.	A
6.	D	7.	B	8.	B	9.	B	10.	D
11.	C	12.	A	13.	A	14.	C	15.	D
16.	A	17.	B	18.	A	19.	C	20.	B
21.	D	22.	C	23.	C	24.	C	25.	B
26.	C	27.	C	28.	C	29.	D	30.	C
31.	A	32.	D	33.	D	34.	D	35.	C
36.	C	37.	B	38.	A	39.	B	40.	C
41.	A	42.	B	43.	B	44.	A	45.	B
46.	D	47.	B						

Chapter 10

Financial Statements Analysis

Answers of Multiple Choice Questions :

1.	D	2.	A	3.	B	4.	C	5.	D
6.	D	7.	B	8.	C	9.	C	10.	D
11.	A	12.	B	13.	D	14.	C	15.	D
16.	C	17.	A	18.	D	19.	D	20.	B

Chapter 11

Tools of Financial Analysis : Comparative Statements

Answers of Multiple Choice Questions :

1.	D	2.	D	3.	D	4.	B	5.	C
6.	C	7.	D	8.	D	9.	C	10.	D
11.	A	12.	C	13.	B	14.	A	15.	C
16.	D	17.	B	18.	A	19.	C	20.	B

21. B 22. C 23. C 24. C 25. D
26. C 27. D 28. C 29. A 30. B
31. A

Chapter 12

Common-Size Statements

Answers of Multiple Choice Questions :

1. D 2. B 3. B 4. C 5. C
6. A 7. D 8. B 9. C 10. D
11. B 12. D 13. C 14. C 15. C
16. D

Chapter 13

Cash Flow Statement

Answers of Multiple Choice Questions :

1. C 2. C 3. B 4. C 5. D
6. D 7. B 8. C 9. B 10. D
11. B 12. D 13. C 14. A 15. D
16. D 17. C 18. A 19. B 20. C
21. C 22. C 23. A 24. C 25. B
26. B 27. C 28. C 29. B 30. C
31. A 32. D 33. B 34. C 35. A
36. A 37. A 38. A 39. C 40. C
41. A 42. D 43. A 44. D 45. C
46. D 47. B 48. D 49. C 50. A

Chapter 14

Ratios Analysis

(A) Answers of CASE-BASED MCQs :

1. (*a*) **Ans.** (*iv*) ₹2,00,000

Hints :

Working Capital = Current Assets – Current Liabilities

Current Ratio of the company is 2.4 : 1, therefore, based on current ratio the working capital is 2.4 – 1 = 1.4

If Working Capital is 1.4, Current Assets $= 2.4$

If Working Capital is 1, Current Assets $= \frac{2.4}{1.4}$

If Working Capital is 2,80,000, Current Assets $= \frac{2.4}{1.4} \times 2,80,000$

$= ₹4,80,000$

Current Liabilities $=$ Current Assets – Working Capital

$= 4,80,000 - 2,80,000 = ₹2,00,000$

(*b*) **Ans.** (*i*) ₹1,60,000

Hint :

Quick Ratio $= \frac{\text{Liquid Assets}}{\text{Current Liabilities}}$

1.6 (Given) $= \frac{\text{Liquid Assets}}{2,00,000}$

∴ Liquid Assets $= ₹2,00,000 \times 1.6 = ₹3,20,000$

Inventory $=$ Current Assets – Liquid Assets

$= ₹4,80,000 - ₹3,20,000 = ₹1,60,000$

(*c*) **Ans.** (*ii*)

Hint : He may purchase goods on Credit for ₹80,000

Answers of CASE-BASED MCQs :

2. (*a*) **Ans.** (*iii*) 3.4 times

Hint :

Interest Coverage Ratio $= \frac{\text{Net Profit before Interest and Tax}}{\text{Fixed Interest Charges}}$

Calculation of Net Profit before Interest and Tax	₹
Net Profit after Interest and Tax	90,000
Add : Tax provided during the year	30,000
Add : Interest on Loan @ 10%	50,000
	1,70,000

Interest Coverage Ratio $= \frac{₹1,70,000}{₹50,000} = 3.4$ times

(*b*) **Ans.** (*ii*) 0.75 : 1

Hint :

Proprietary Ratio $= \frac{\text{Shareholder's Funds}}{\text{Total Assets}}$

Shareholder's Funds =	₹
Equity Share Capital	2,00,000
5% Pref. Share Capital	60,000
General Reserve	1,20,000
Surplus i.e. net profit after Interest and Tax	90,000
	4,70,000

Total Assets $=$ Fixed Assets + Current Assets

$= ₹5,05,000 + ₹1,20,000 = ₹6,25,000$

Proprietary Ratio $= \frac{₹4,70,000}{₹6,25,000} = 0.75 : 1$

Answers of CASE-BASED MCQs :

3. (*a*) **Ans.** (*ii*) 2 : 1

Hint :

Total Assets to Debt Ratio $= \frac{\text{Total Assets}}{\text{Long term Debts}}$

$$\text{Long term Debts} = \text{Long term Borrowings} - \text{Long term Provisions}$$

$$= ₹5{,}00{,}000 + ₹3{,}00{,}000 = ₹8{,}00{,}000$$

$$\text{Total Assets to Debt Ratio} = \frac{₹16{,}00{,}000}{₹8{,}00{,}000} = 2 : 1$$

Note : 6% Debentures are already included in Long term Borrowings.

(*b*) **Ans.** (*iv*) 1.33 : 1

Hint :

$$\text{Debt Equity Ratio} = \frac{\text{Long term Debts}}{\text{Shareholder's Funds}}$$

$$= \frac{₹8{,}00{,}000}{₹6{,}00{,}000} = 1.33 : 1$$

(*c*) **Ans.** (*ii*) Conversion of Debentures into shares.

Answers of CASE-BASED MCQs :

4. (*a*) **Ans.** (*ii*) ₹30,00,000

Hint :

$$\text{Debt Equity Ratio} = \frac{\text{Long term Debts}}{\text{Shareholder's Funds}}$$

$$1.2 = \frac{36{,}00{,}000}{\text{Shareholder's Funds}}$$

$$\text{Shareholder's Funds} = \frac{36{,}00{,}000}{1.2} = ₹30{,}00{,}000$$

Note : 6% Debentures of ₹6,00,000 are already included in Long-term Borrowings of ₹36,00,000

(*b*) **Ans.** (*iv*) ₹75,00,000

Hint :

$$\text{Proprietary Ratio} = \frac{\text{Shareholder's Funds}}{\text{Total Assets}}$$

$$40\% = \frac{30{,}00{,}000}{\text{Total Assets}}$$

$$\text{Total Assets} = 30{,}00{,}000 \times \frac{100}{40} = ₹75{,}00{,}000$$

Answers of CASE BASED MCQs :

(*a*) **Ans.** (*iii*) 2.34 times

Hint :

	₹
Current Assets :	
Trade Receivables	2,00,000
Inventory	1,49,000
Cash and Bank Balance	36,000
Marketable Securities	80,000
Prepaid Rent	3,000
	4,68,000
Current Liablities :	
Trade Payables	1,40,000
Bank Overdraft	20,000
Outstanding Expenses	10,000
Provision for Tax	30,000
	2,00,000

$$\text{Current Ratio} = \frac{\text{Current Assets}}{\text{Current Liabilities}} = \frac{4,68,000}{2,00,000} = 2.34 \text{ times}$$

(*b*) **Ans.** (*ii*) 1.58 times

Hint : **Quick Assets :**

	₹
Trade Receivables	2,00,000
Cash and Bank Balance	36,000
Marketable Securities	80,000
	3,16,000

$$\text{Quick Ratio} = \frac{\text{Quick Assets}}{\text{Current Liabilities}} = \frac{3,16,000}{2,00,000} = 1.58 \text{ times}$$

(*c*) **Ans.** (*ii*) 4 times

Hint :

Gross Profit is 25% on Revenue from Operations

Hence, Goods costing ₹75 must have been sold for ₹100

$$\text{Revenue from Operations} = 6,30,000 \times \frac{100}{75} = ₹8,40,000$$

$$\text{Trade Receivable Turnover Ratio} = \frac{\text{Revenue from Operations}}{\text{Trade Receivables}}$$

$$= \frac{8,40,000}{2,10,000} = 4 \text{ times}$$

Answers of CASE-BASED MCQs

6. (*a*) **Ans.** (*iv*) 74%

Hint :

$$\text{Operating Ratio} = \frac{\text{Cost of Revenue from Operations} + \text{Operating Expenses}}{\text{Net Revenue Operations}}$$

$$\text{Cost of Revenue from Operations} = \text{Net Revenue from Operations} - \text{Gross Profit}$$

$$= ₹25,00,000 - 40\% \text{ of } ₹25,00,000 = ₹15,00,000$$

$$\text{Operating Expenses} = \text{Employee Benefit Exp.} + \text{Depreciation} + \text{Selling Exp.}$$

$$= ₹2,00,000 + ₹50,000 + ₹1,00,000$$

$$= ₹3,50,000$$

$$\text{Hence, Operating Ratio} = \frac{₹15,00,000 + ₹3,50,000}{₹25,00,000} = 74\%$$

(*b*) **Ans.** (*i*) 26%

Hint :

$$\text{Operating Profit} = \text{Gross Profit} - \text{Operating Expenses}$$

$$= ₹10,00,000 - ₹3,50,000 = ₹6,50,000$$

$$\text{Operating Profit Ratio} = \frac{6,50,000}{25,00,000} \times 100 = 26\%$$

Answers of Multiple Choice Questions

1. B 2. B 3. C 4. C 5. D
6. C 7. C 8. B 9. A 10. B
11. C 12. A 13. D 14. B 15. C
16. B 17. D 18. A 19. D 20. C

21.	D	22.	B	23.	C	24.	B	25.	C
26.	B	27.	A	28.	D	29.	D	30.	B
31.	A	32.	C	33.	C	34.	B	35.	D
36.	B	37.	C	38.	C	39.	D	40.	C
41.	C	42.	B	43.	C	44.	A	45.	B
46.	C	47.	D	48.	A	49.	B	50.	D
51.	C	52.	D	53.	B	54.	A	55.	C
56.	A	57.	C	58.	B	59.	B	60.	C
61.	D	62.	A	63.	C	64.	D	65.	C
66.	D	67.	D	68.	C	69.	B	70.	A
71.	C	72.	D	73.	B	74.	C	75.	A
76.	B	77.	C	78.	B	79.	D	80.	B
81.	A	82.	B	83.	A	84.	C	85.	C
86.	A	87.	D	88.	A	89.	B	90.	B
91.	A	92.	C	93.	B	94.	C	95.	B
96.	B	97.	B	98.	C	99.	D	100.	A
101.	B	102.	A	103.	A	104.	B	105.	D
106.	D	107.	D	108.	A	109.	B	110.	C
111.	B	112.	C	113.	B	114.	A	115.	B
116.	D	117.	D	118.	A	119.	B	120.	A
121.	C	122.	B	123.	B	124.	B	125.	A
126.	D	127.	A	128.	C	129.	D	130.	B

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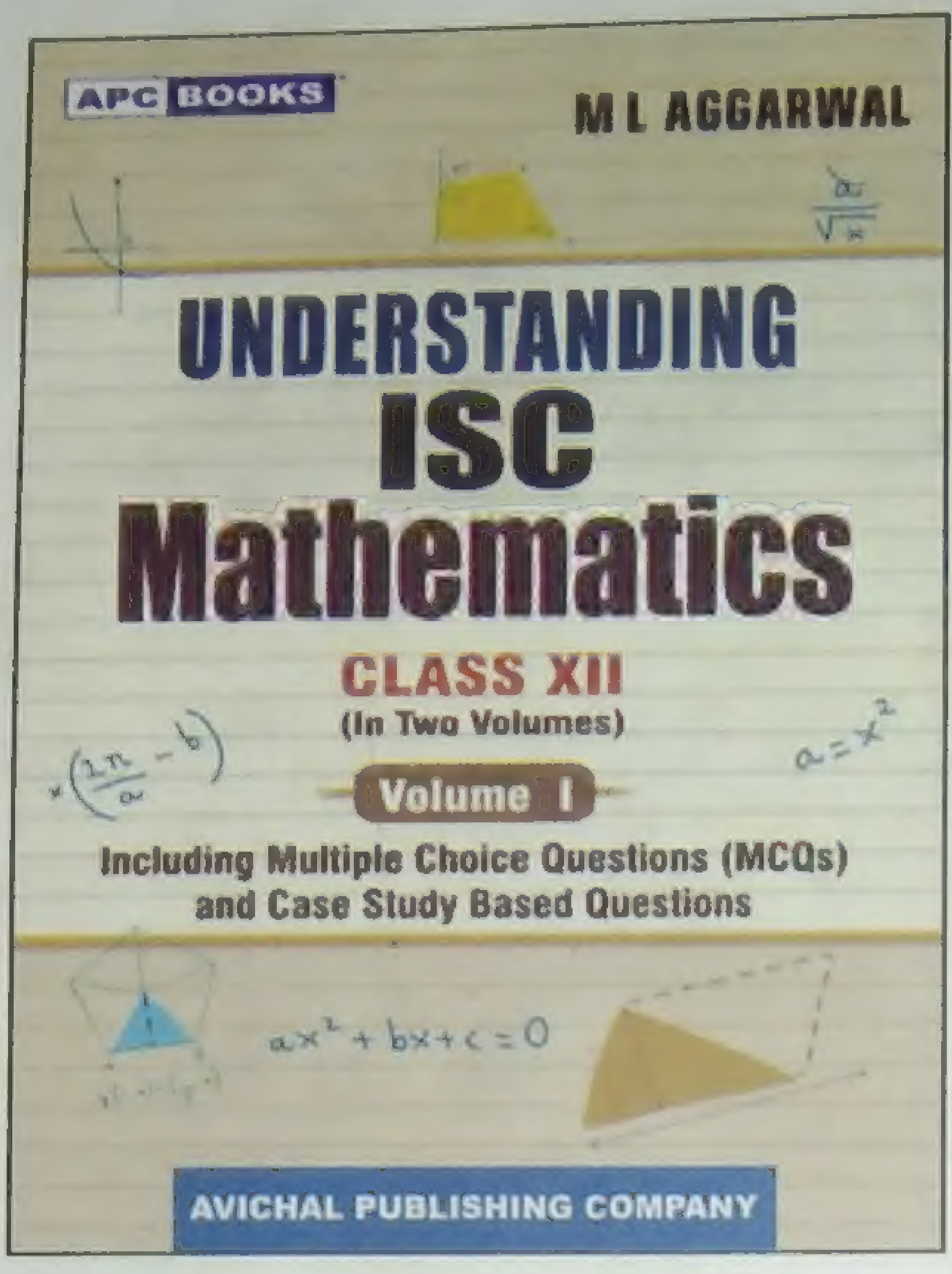

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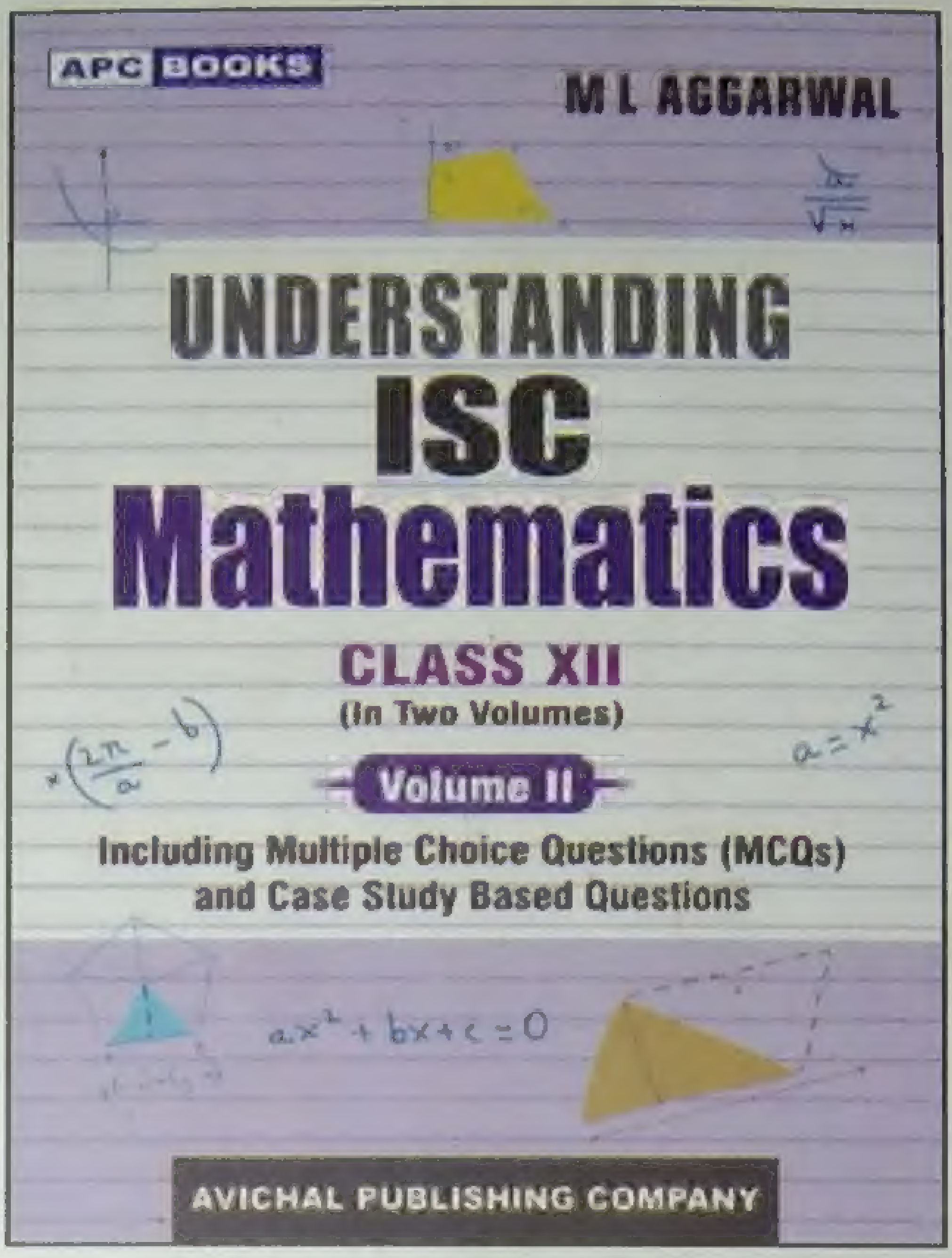

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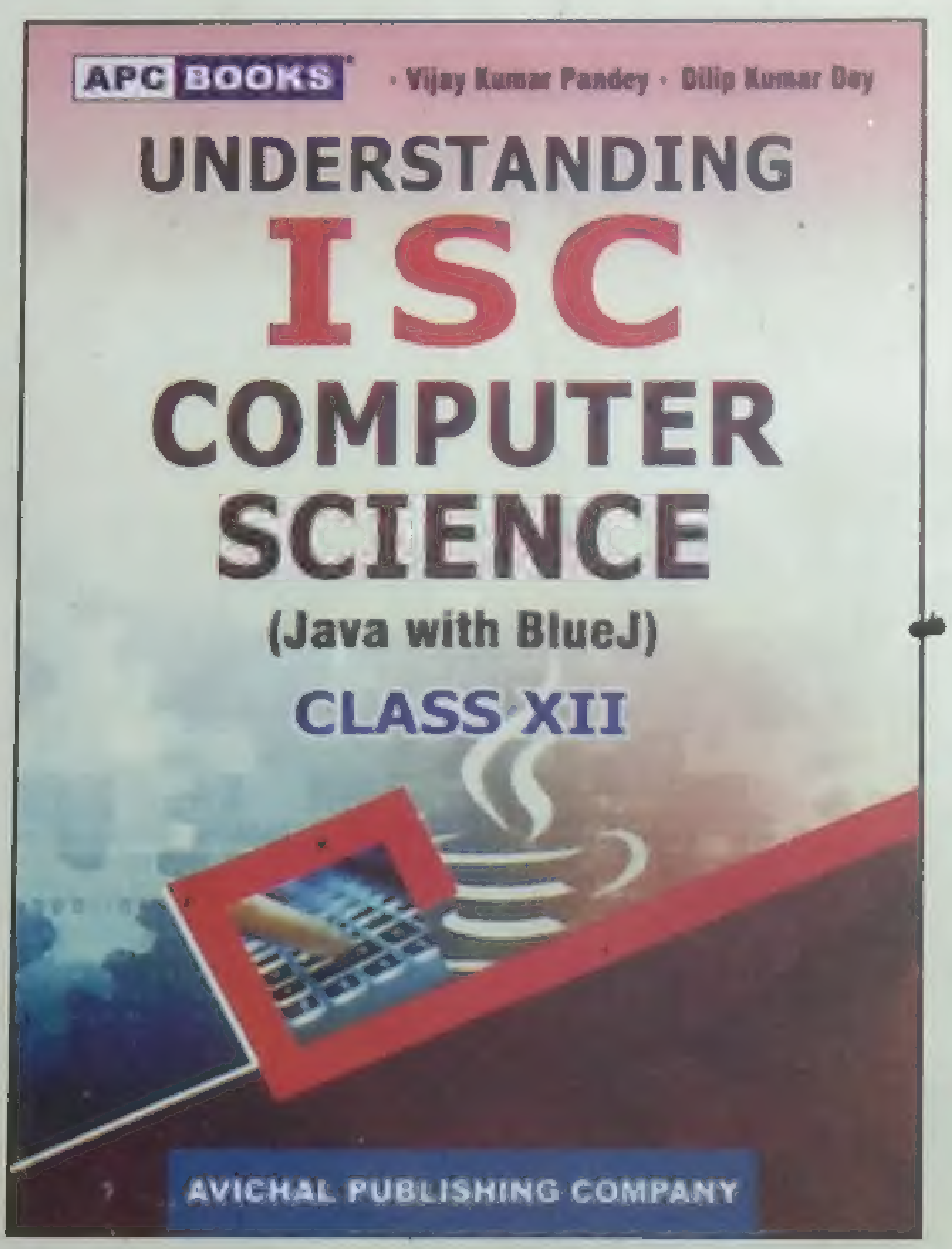

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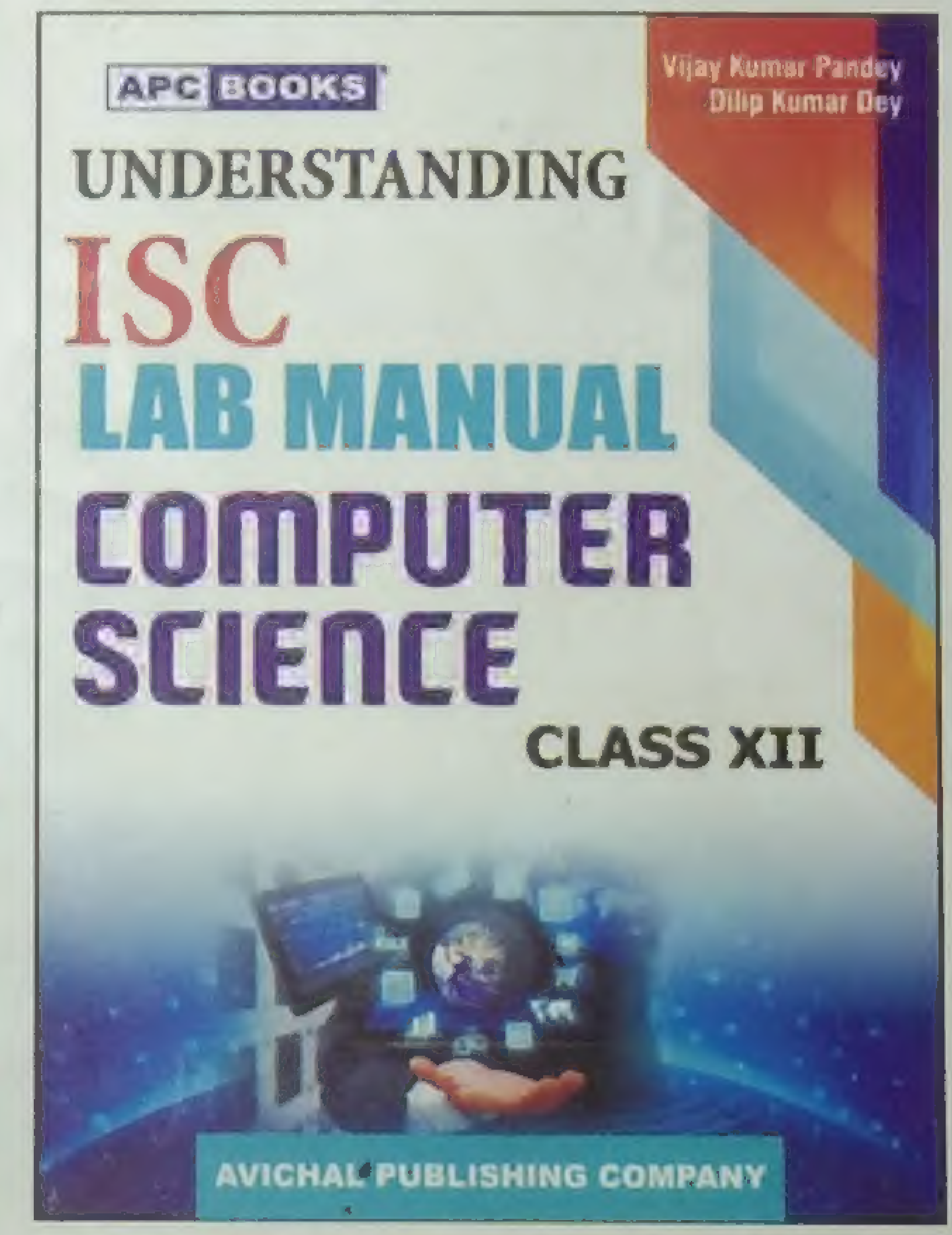

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